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October 2024

Eastern EU members secure key portfolios in new European Commission

Turkey will deepen ties with East while facing West, says Erdogan

Who is Ukraine's new Foreign Minister, Andrii Sybiha?

EUROPE HAS LOST ITS COMPETITIVE EDGE

Have lab-grown diamonds changed the diamond industry forever?
P10

Central Asia is a big winner from the Ukraine war
P58

Russia gets ready to rebuild its military stockpile
P68

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COMPANIES & MARKETS

COVER FEATURE


54


61


66

Martin Gauss: "With the new modern fleet, we are at the forefront of the industry, a fact that I am very proud of." / airBaltic

INTERVIEW

Martin Gauss, airBaltic CEO

Linas Jegelevicius in Vilnius

Latvia's airBaltic, the leading airline in the Baltic states, has been in the news recently, amid talk of an initial public offering (IPO), with Germany's Lufthansa taking a stake as a lead investor beforehand. The state-owned airline has confirmed that it is in talks with one strategic investor. To find out what the airline is up to, *bne IntelliNews* sat down with Martin Gauss, airBaltic's CEO.

Gauss shied away from discussing the IPO directly but was keen to talk about the turnaround story at airBaltic over the past decade. airBaltic currently operates over 130 routes from Riga, Tallinn, Vilnius, Tampere, and seasonally from Gran Canaria, connecting to various destinations across Europe, the Middle East, North Africa, and the Caucasus. It already has code-sharing and wet leasing agreements with Lufthansa.

"Indeed, there is a lot of discussion and talk about our potential IPO, but we are not commenting on it yet, regulation does not permit me to – the earliest time we potentially could do an IPO is the second half of 2024 or in 2025," Gauss says, emphasising that "it is not happening overnight",

Your IPO quest comes amid news that airBaltic saw a turnover of €339.3 million in the first half of this year, but you posted a significant loss of €88.8 million, a stark contrast to the same period last year when the company posted a profit of €14.6 million. Lufthansa, Air France, KLM also saw worse figures in the first half-year. What is this decrease due to? Can we speak of a slight overheating effect in the aviation market?

Generally, we are seeing the opposite – we reported many higher numbers than a year before. We are not seeing the overheating effect. I think that, in general, this year, for the first time, all Europe is coming [back] to the numbers of the pre-pandemic level in 2019.

In fact, airBaltic looks better than many others – we had a higher Ebitdar margin. Our airline is definitely in growth, using an aircraft model which does not exist in Europe: The airBaltic fleet consists of a single aircraft type – the Airbus A220-300 – and the airline currently operates 48 aircraft of this type. airBaltic plans to operate a fleet of 100 A220-300s by 2030.

Looking at the first half-year report, I'd also like to pay attention to that, for the first time, we had a breakout between two business segments that recovered. On one hand, we are a full-service legacy kind of airline, with an ultra low-cost environment, which is ensured with the very modern mentioned aircraft. And on the other side, we have wet lease business, which is traditionally done with old aircraft, but, at airBaltic, we do it very successfully using our A220-300s and we do it in the same service concept, which puts us at No4 airline worldwide, considering the number of flights conducted in the segment. So having these two successful sectors combined moves the airBaltic business success story forward.

airBaltic also continues to report growth in its passenger numbers. In August, the airline carried more than half a million passengers, marking a 13 per cent increase compared to the same period last year. In the previous month, airBaltic performed 4,510 flights, showing a 6 per cent increase from August 2023. Furthermore, for the second month in a row, in August airBaltic reached the highest load factor in the company's history – 89.8 per cent, which is a 6.6 percentage point increase compared to the same period last year.

Interestingly, if we were to look at our growth geography, we will see that [this is happening] mainly out of the Baltic States, where we are leader, and, looking forward, we will certainly see new record passenger numbers. So, overall, as an airline, considering the difficult environment – airlines are reporting not so good numbers now – due to its growth, airBaltic is enjoying a very good position and a very good outlook ahead.

What poses the biggest challenge for the post-pandemic aviation industry?

Of course, the biggest recent challenge was covid, followed by war in Ukraine. Looking wider geographically, the geopolitical impact of the war, as well as the conflict in the Middle East – we had to suspend our flights to Tel Aviv for some time as the result – was significant.

Also, the economies, which are not growing, pose a challenge. If the European economies will not be growing like the other economies all over the world, the European aviation industry will understandably show worse numbers. But, speaking of the large picture, the industry and especially our airBaltic is enjoying modernisation while going to net zero, meaning cutting carbon emissions. Targeting the goal, with the new modern fleet, we are at the forefront of the industry, a fact that I am very proud of.

However, there are around 22,000 jets that still need to be replaced with modern ones. On top of that, the industry deals with the issues of supply chain or even the challenge of aircraft deliveries. As far the latter is concerned, we are not affected by it, but, like many others, we are affected by, say, engine supply.

Speaking of sustainability, when will airBaltic will have its maiden electric-powered flight?

There are no orders for electric aircraft in our order book. Yet we might have an electric aircraft in our own pilot academy in the future. No doubt, the first all-electric aircraft will be way smaller in size, and we are closely following the development. As I said, A220-300 is the latest technology.

I remember the old days when airBaltic prided itself in being the most punctual airline, but, nowadays, it seems all carriers shun the issue, which is still very important to many. Is aircraft punctuality gone for good?

(Grins) It is not true that punctuality is not important anymore. For example, last week [September 2-8], our punctuality was 70 per cent, meaning that, of 100 aircraft, 70 took off on time, which, I think, is not bad. If, say, you go from Frankfurt to Los Angeles, which is a 12-hour flight, and you have one-hour flight delay, but then you fly safe and with comfort and arrive a half hour late and still can do your business as planned, does it matter a lot?

But, for years, delays, especially in summer in Europe, are mostly driven by shortage of air traffic control staffing, which is primarily related to not having a single European sky – one of the largest issues for the last 25 years. Besides, we're seeing an increasing issue of labour shortages in the entire service industry, including airports. We can come on time, but we depend on local services in offloading the baggage, there might be not enough staff at the security desk and so on. That's the European-wide problem, which was especially caused by the covid pandemic, during which many people, due to the travel restrictions, had to look for jobs in other sectors and they kept their new jobs when the pandemic was over.

airBaltic has offered the Lithuanian and Estonian governments to buy its shares. Did you hear back from them?

To be exact, the Lithuanian Ministry of Transport and Communication and a respective Estonian ministry reached out to us, asking us to meet their officials and explain how it would look like if the two Baltic governments were interested in buying our shares. All I said, and I'd say this to anyone who would be interested in our shares, was to get in touch with our shareholders to speak about this. But when we go IPO, this could be done either in the preparation phase after we announce it, or later, after the IPO has been announced, and shares are on the stock exchange. However, speaking of the two governments, their intentions were not further discussed.

What are you proud of most as the airBaltic CEO?

When I came to airBaltic in November 2011, we had a fleet of old and overpriced Boeings and Fokker 50 aircraft. The airline was little known and, now, it is known internationally and highly profitable, most importantly, the true flagship of Latvia and the entire Baltics. ●

Dolomite mine owned by Orban's father supplies Hungary's largest railway project

Hungarian Prime Minister Viktor Orban (right) with Chinese President Xi Jinping. / bne IntelliNews

Tamas Csonka in Budapest

Dolomit Ltd, a company majority-owned by Hungarian Prime Minister Viktor Orban's father, Gyozo Orban, supplied over 200,000 tonnes of railway stone for the Budapest-Belgrade railway project between 2022 and 2023, reportedly at above-market prices, according to internal documents obtained by 444.hu.

The Budapest-Belgrade railway upgrade, Hungary's largest railway project, is part of China's Belt and Road Initiative (BRI). Its goal is to improve trade and transportation links between Europe and Asia.

The $3bn project, which began in 2017, has faced scrutiny due to its high costs and lack of transparency and for the strategic implications related to China's growing influence in the region. Critics also question the commercial viability of the railway, as it primarily serves freight traffic from China while incurring significant costs for Hungary and Serbia.

Hungary is financing its share of the railway development through a Chinese loan.

The completion of the Serbian section is expected by 2025, with the Hungarian section projected to be finished soon after. The project has suffered delays due to technical, regulatory and financial complexities.

Critics say the involvement of the prime minister's family exemplifies crony capitalism at its worst in Hungary and illustrates well which business circles benefit most from large-scale infrastructure projects.

Despite narrowing fiscal manoeuvre room and the postponement of some state-backed projects, the government recently awarded a HUF440bn (€1.12bn) road construction project to Duna Aszfalt, a company owned by businessman Laszlo Szijj, who is also close to the ruling regime.

Dolomi is majority-owned by Orban's father, with the Prime Minister's brother also holding stakes in the company. The firm has supplied materials from its mine in Gant, central Hungary, for several state or EU-funded infrastructure projects, including sewerage works, road, and railway construction in the past. According to publicly available data, Orban's father has received more than HUF10bn in dividends from the mining business over 10 years.

The crushed dolomite for the Budapest-Belgrade railway project was ordered by V-Híd, a company owned by Lorinc Meszaros, reportedly Hungary's richest man and another tycoon close to the regime, and Chinese firm China Tiejiuju Engineering & Construction. The stone was used to create the load-bearing layer under the tracks.

"Dolomi is majority-owned by Orban's father, with the Prime Minister's brother also holding stakes in the company"

While the exact total amount of material supplied from the Gant mine and the payment received are not specified in the obtained documents, one document reveals that the Chinese contractor planned to conclude a contract worth HUF1bn gross for the delivery of "at least 100,000 tonnes" of stone, with prices reportedly higher than those charged by competitors.

The total sum paid to Dolomit remains unclear, as the companies involved declined to respond to inquiries. This lack of transparency raises further questions about the financial arrangements surrounding the project.

This situation underscores ongoing concerns about potential conflicts of interest and the distribution of public funds in Hungary's infrastructure projects, particularly those involving international partnerships and substantial investments. ●

The new Uzbek-Afghan free economic zone on the border promotes better ties with the Taliban

Emma Collet in Termez

Uzbekistan is once again asserting itself as one of the most active countries in Central Asia in its pragmatic rapprochement with the Taliban in Afghanistan. To minimise the risks posed by the unpredictable Islamist regime, which has been on the doorstep of its borders for three years now, Tashkent has just completed the construction of a sparkling new shopping centre, accessible from both sides of the border via visa-free access for Afghan and Uzbek traders.

Those from Afghanistan will travel a few kilometres along a 'green corridor', braving the recurrent little sandstorms on the Uzbek-Afghan border, that will take them directly to the "Airitom free zone", where they can stay for 15 days without a visa and enjoy tax-free trading. The 36 hectares place is located on the Uzbek side of the 'Freedom Bridge', spanning the muddy waters of the Amu-Darya that separates the two countries -- the same bridge retreating Soviet troops used in 1989 after their defeat in the Afghan war.

The Airitom zone, named after one of the districts of Termez, the regional capital of the southern Surkhandaryo region, which is closest to the Afghan border, was inaugurated on August 29, in the presence of Uzbek Prime Minister Abdulla Aripov. He invited a Taliban delegation, as well as ministers and diplomats from Kyrgyzstan, Kazakhstan and Azerbaijan, showing that the zone represents a new step towards another act of normalising the Taliban in Central Asia, with Uzbekistan taking the lead.

"The project has already been in the pipeline since 2020. When the Taliban came to power we had to continue discussions with them. It went rather well," explains Kodis Parpiyev, the manager of the commercial complex.

On August 18, the Uzbek prime minister even went so far as to travel to Kabul to meet his Taliban counterpart and sign a number of commercial and investment contracts worth $2.5bn, becoming the first head of government in the world to visit the Afghan capital. However, this first visit did not come as much of a surprise on the international stage. Relations between Afghanistan and Uzbekistan go back a long way, developing as soon as President Shavkat Mirziyoyev came to power in 2016, when he made opening up Afghanistan a top priority, turning the page on the quarter-century of economic and diplomatic autarky under President Islam Karimov.

Since the Taliban's return to power three years ago, President Mirziyoyev has stressed that instability in Afghanistan is the main security risk in Central Asia. Uzbekistan has taken the initiative to improve relations between the two countries, which are separated by a short stretch of border some 137 km to the south, near the regional capital Termez.

Between the two ultra-militarised border checkpoints, where queues of goods lorries line up on the Uzbek side to reach Afghan territory, now lies this massive tax-free economic zone, an architectural UFO with brand new buildings straight out of the ground. At a cost of $70mn, the Airitom complex was built by the private holding Afka, owned by Jahongir Artikkhodjayev, business tycoon and former mayor of Tashkent. The Uzbek government provided a $20mn credit line over five years to support its construction, which explains the presence of the state-of-the-art Afka medical hospital, and of several Afka subsidiary stores, omnipresent in the commercial space of the economic zone.

In addition to the hospital designed to attract Afghans seeking medical treatment – a crucial service given the dearth of modern healthcare facilities in Afghanistan, the complex includes a Hilton hotel and a luxury restaurant serving Turkish and Uzbek specialties. But most importantly, four large blocks are intended to house around 300 retailers, specialising in fresh produce, building materials and automotive products.

Some Uzbek citizens are already buying and negotiating stands to set up their business, sniffing out the good opportunity offered by the creation of this tax-free zone,

Uzbekistan has opened the $70mn Airitom free zone on the border with Afghanistan and promote trade and improve ties with its unstable neighbour. / bne IntelliNews which aims to attract buyers not just from Afghanistan but from all the countries in the region. Bismallah Yusufi, a Termez resident of Afghan origin, has already set up a branch of his lighting shop in one of the malls. He rents the 100-square metre space for $1,000 a month. "For the moment, business isn't good because the Afghans haven't arrived yet," he says.

"The businessmen who are flocking to the new economic zone are mainly Uzbeks of Afghan origin"

Indeed, the huge trade and exchange zone looks like a ghost town, as in mid-September the Taliban had not yet authorised Afghan traders to cross the green corridor into the economic zone. "It's only a matter of weeks now," says a slightly distraught Kodis Paripyev. The zone is designed to generate $1.4mn in monthly trade, according to the complex's director, who is fairly optimistic about its potential, and to attract more than 1.5mn people a year.

For $80,000, Mukhamad Oqsoqol, a Termez businessman, bought a site on the corner of one of the large commercial blocks. "For the moment, I don't really know what I'm going to sell, because the list of products isn't clear yet," explains the entrepreneur, who runs several shops selling manufactured goods in Termez. According to the authorities, this information should be released in October, possibly.

The businessmen who are flocking to the new economic zone are mainly Uzbeks of Afghan origin. The town of Termez is home to a large diaspora of Afghans, most of whom settled here in the 1990s after the Taliban first took power in Afghanistan and have since been joined by a few dozen compatriots who fled the Taliban in 2021. "There are 400 Afghan companies in Termez," says Otabek Tursunov, Termez hokimyat's (mayorial) deputy. "Most of them are very involved in trade with Afghanistan," he adds.

Many of them are then looking favourably on the brand new commercial centre at the border, according to several representatives of the Afghan diaspora in Termez. The modernity of the economic zone, just a few hundred metres from an Afghanistan ravaged by an unprecedented economic and social crisis, is impressive and illustrates Tashkent's efforts to adapt to the challenges posed by its underdeveloped, Islamist-ruled neighbour.

On the floor of one of the shopping malls a university has also been created and is ready to welcome 200 Afghan students per term, who will be housed and fed on the premises of the business complex. A subsidiary of Central Asia University, the courses will be taught in English and Pashto, and will cover the basics of business. However, only men will be allowed to attend, reflecting the restrictions imposed on women's education under the Taliban regime.

The free trade zone is expected to employ around 3,000 people, with a third of the jobs reserved for Afghans. To make things easier, a bus service between Mazar-e-Sharif and the free zone is being prepared so as to provide daily transport for Afghan workers.

"Afghans who want to set up their business here will have access to subsidies," explains Kodis Papriyev. But as well as Uzbek companies and a few Afghan brands, international groups have also been invited. On the site, we can already see a Russian truck stand in front of one of the malls. "In addition to the Russians, Ukrainians and Belarusians have already shown interest in buying a stand. But it's mainly the Chinese who are the most interested," explains Kodis Parpiyev.

There is no doubt that the new economic zone will give a further boost to cross-border trade, which has continued to accelerate between Uzbekistan and Afghanistan, despite the arrival of the Taliban. "Here, the 'Friendship Bridge' was only closed for three days, just long enough to clear the bridge of the cars of Afghans who had fled the Islamist regime across the border with Afghanistan", recalls Nodirbek Djalilov, director of the Termez Cargo Centre, a logistics centre for cross-border trade on the Uzbek-Afghan border. According to him, between 100 and 150 lorries cross the border every day on both sides, not counting the 500 to 1,000 tonnes of humanitarian aid sent daily by the UN, which continues to pass through Uzbekistan.

From Afghanistan, dried fruit and a few fizzy drinks cross the border, while from Uzbekistan, flour, wheat and above all fuel head south. 30% of the lorries go to Pakistan, a country that has the advantage of having global seaports for the countries of Central Asia.

"The new economic zone will create more competition in the goods trade," concludes Nodirbek Djalilov. This can only bring positive things to business and to peace." ●

"The modernity of the economic zone, just a few hundred metres from an Afghanistan ravaged by an unprecedented economic and social crisis, is impressive and illustrates Tashkent's efforts to adapt to the challenges posed by its underdeveloped, Islamist-ruled neighbour"

Central Asian leaders seek German expertise to build manufacturing base

Eurasianet

Central Asian leaders sent German Chancellor Olaf Scholz a clear and consistent message during his three-day visit to the region: "To get, you've got to give."

The five Central Asian heads of state gathered in the Kazakh capital Astana on September 17 for a meeting with Scholz, with discussions focusing on expanding trade between the West and Central Asia. Germany is particularly interested in boosting natural gas imports from the region as part of a continuing pan-European Union effort to pivot away from Russian energy. No specific deals were announced at the meeting's conclusion, but all sides were upbeat about the future, holding out the possibility that agreements can be reached in the not-too-distant future.

"Exchanges between our societies have never been so close, and they are constantly growing," the DPA news agency quoted Scholz as saying.

The meeting's host, Kazakh President Kassym-Jomart Tokayev, reciprocated the goodwill, saying "the thorough exchange of views that took place reinforced the mutual interest of the leaders in further deepening cooperation." He also emphasised that energy issues will play a "key role" in guiding relations.

Tokayev's remarks during the meeting offered a rough roadmap for future trade relations. He indicated Kazakhstan and other regional states would be more than happy to help Germany, along with other EU states, meet its energy needs. But Central Asia is looking for something more than just money in return for energy exports.

Describing Germany as a world leader in "the field of economic and technological innovation," Tokayev said Kazakhstan and other Central Asian states want to tap into German knowhow with the aim of promoting the "localisation of production and the production of products with high added value." Among the economic sectors he mentioned that could benefit from German technology transfers were finance, agriculture, transit logistics and information technology.

Tokayev also made it clear that Kazakhstan sought German expertise, along with investment, to develop Central Asia's green energy agenda, specifically mentioning an initiative undertaken by Azerbaijan, Kazakhstan and Uzbekistan to develop solar- and wind-power plants to generate electricity for export to the EU. "We invite our German partners to consider the possibility of participating in this strategic project," Tokayev dropped a not-so-subtle hint.

Before visiting Kazakhstan, Scholz stopped in Uzbekistan, where a similar "give-get" dynamic governed his talks in Samarkand with Uzbek President Shavkat Mirziyoyev. The chief outcome was a politically expedient deal under which Germany can send would-be Afghan migrants to Uzbekistan for eventual repatriation to Afghanistan; in return, Berlin agreed to accept Uzbek skilled workers to fill employment opportunities in Germany.

German Chancellor Olaf Scholz speaks with Kazakh President Kassym-Jomart Tokayev during a meeting with German business executives in Astana on September 17. / akorda.kz

"With our agreement ... we are enabling people with great talents to enter our country. Also, we committed to un-bureaucratic processes so that those who cannot stay in our country must go back," Scholz wrote on his X channel.

For Scholz, the agreement shows that his embattled Social Democrat-led government is addressing the migration issue at home. Simmering dissatisfaction with the government's handling of migration has caused an erosion of popular support for his coalition and was widely cited as a major factor in the strong performance of the far-right Alternative for Germany (AfD) Party in recent state elections.

The deal is also a win for Mirziyoyev, whose administration is trying to shift Uzbekistan's economic orientation from being mainly a producer of raw materials to a manufacturer of finished goods. As part of the overhaul, the government is attempting to reorganise the country's labour market, in particular labour migration, by creating more opportunities for skilled workers abroad.

By extension, the German-Uzbek agreement can potentially benefit the militant Taliban leadership in Kabul, which, since regaining power in 2021, has sought to gain international recognition of its rule. Tashkent, of late, has sought to engage the Taliban, aiming to stabilise conditions along Uzbekistan's southern border, as well as gain some say over the completion and operation of the controversial Qosh-Tepa canal project. As part of its engagement drive, Uzbekistan has agreed to process comparatively small amounts of Afghan crude oil to help meet domestic needs in Afghanistan. The Uzbek government also recently agreed on a investment deal worth potentially up to $2.5bn with the Taliban.

If the Taliban accepts the return of Afghan nationals sent from Germany to Uzbekistan, the militant movement would demonstrate that it can act as a responsible international actor, potentially helping its efforts to legitimise its rule. ●

This article first appeared on Eurasianet.

Have lab-grown diamonds changed the diamond industry forever?

Richard Chetwode in London

Kodak never saw it coming either. Since early 2022, the price of polished natural diamonds has fallen approximately 40% and the industry is being buffeted by negative economic headwinds, an excess of mine supply and too much stock in the cutting centres. However, there is one statistic that cannot be ignored: around 50% of Diamond Engagement Rings purchased in the United States now contain a Lab Grown Diamond (LGD). Is this just another cyclical downturn or are we in the middle of a major structural change?

Diamonds were once the preserve of royalty and the uber-wealthy, but the diamond market has evolved over the past 80 years into more of a mass market product with democratisation of the diamond consumer. Since the late 1970s most polished diamonds below 5 carats were priced against the 4 'C's' (carat, clarity, colour and cut), which led to standardised pricing in the form of polished diamond pricing lists. Up until the turn of the century these lists were primarily available in the wholesale market, but the arrival of internet pricing soon gave the consumer access to that same standardised pricing. In a world where everyone knows the price of everything, branding is the only differentiator. Without a differentiator, commoditised products end up selling for the lowest price.

It was why one of the questions that De Beers tried to answer when it changed its business model 25 years ago was: "How do you take a necessity (the diamond) priced like a commodity and market it as a luxury priced like a brand?"

Unfortunately, that question remains unanswered. The industry did create hundreds of so-called 'brands'; origin, cut, settings, etc; the problem was that very few of them were real "brands". If something does not sell at a premium, it's not a brand, and most natural diamonds sell at a discount, yet the more that the industry was unable to achieve a premium, the more it becomes fixated with talking about the "product" when the luxury world has spent the last 25 years talking about "values".

The challenge for most jewellers is not making a sale, it is making a reasonable margin. Ask a jeweller what they are selling and if they reply "VS1, G-H colour, loose polished, 1-caraters" then the most relevant word in their business will be "discounting", because what they are selling is a commoditised version of "crystallised carbon." There is no differentiator.

The LGD industry realised that to succeed it simply needed to persuade consumers that natural diamonds and LGDs were the same – "optically, physically and chemically", but to also position them as "slightly cheaper". They could then ride on the back of 80 years of De Beers diamond advertising differentiate themselves by claiming that LGDs were "conflict free".

A larger "ethical" LGD for the same money as a natural diamond or pay less for the same size, created a money printing machine for everyone involved. And it's no surprise that LGDs real success has been in the United States, because historically America has always been a "discount market", and "larger for less" plays to that tune.

If all you want in a diamond is the sparkle, then they are in essence the same. Except there is a very real difference between the two, which is why some LGD executives insist on calling natural diamonds "earth mined" diamonds, because "natural" is exactly what differentiates them. The story of their age, rarity, origin; their social and economic contribution but above all, their "social purpose". It was the failure of the natural diamond industry to tell that story which opened the door to LGDs.

When LGD production exploded, wholesale prices collapsed to around a 95% to 98% discount to their natural diamond equivalent. Prices vary according to quality, but anecdotal evidence suggests that today in the wholesale market, it is possible to buy a single polished LGD for $150 a carat, buy in volume and its possible to pay as low as $80 a carat.

Many retailers have also dropped their LGD prices, but by no means as far, and even pricing LGD at a 20-40% discount to their natural diamond equivalent can still leave a very significant margin. Pandora will sell you a 1-carat LGD ring for $1,950. Helzberg Jewellers (a Warren Buffet company) will sell you a similar LGD for $1,999. It's very likely that some in the LGD industry are making a gross margin of 200%, some much more for a product that Signet Jewellers sensibly cautiones it customers "Their relative abundance may not ensure the value will hold over time".

Whatever happens to future LGD retail prices, the category has got itself into the American consumer psyche and that won't easily change, although there are also two sides to this story. I heard of a jeweller who was recently asked by a HNWI to make a replica of her 8-carat natural diamond ring so she could wear it travelling. The original ring cost $500,000 but he sourced an equivalent LGD for $5,000, and apparently she was absolutely thrilled with it. The question is, will she buy natural again? On the other hand, if in the future a consumer could buy (for example) a 2-carat LGD engagement ring for below $200, how pleased would their fiancé be to receive it – Walmart recently had a 2-carat LGD ring for sale for only $257. How romantic!

The US bridal market (size over quality) is dominated by larger, lower quality diamonds. Since similar sized LGDs are cheaper (or you get a much better quality LGD), either that market disappears, or demand only reappears aner prices have fallen sharply (already happened). It is also likely that LGDs will replace small, lower quality natural diamonds in fashion jewellery – as they may replace the smaller stones in high-end pieces of natural diamond jewellery. Diamond mining companies whose profitability rely on these

Artificial diamonds are chemically and physically indistinguishable from "earth diamonds" but they are also much cheaper. That is causing a revolution in the diamond business. / bne IntelliNews

categories of diamonds probably need to find a new value proposition, or their days may be numbered.

For those in the natural diamond industry who can adapt, there is huge potential. For those that don't, as the saying goes, "Kodak never saw it coming either".

Except Kodak did see it coming; they just didn't know what to do about it. Kodak was killed off by digital photography which ironically, they invented, patented, but didn't know how to exploit it, so they franchised the technology and made a fortune until their patents expired, and then went bust. Have LGDs done the same to natural diamonds? "No", the opposite; their success is forcing a complacent industry to change. Have they changed the paradigm? "Completely". ●

Richard Chetwode holds a number of non-executive roles in the diamond and property industry. He is a part-time journalist and is currently writing a book on the diamond industry in World War II. All the opinions in this article are his own but while efforts have been made to ensure the accuracy and reliability of the information provided in this article, neither can be guaranteed. and information in this article is strictly for informational purposes and should not be considered investment or financial advice. Consult your investment professional before making any investment decisions. He is non-executive chairman of Namibian-based Trustco Resources and has previously worked for De Beers, Harry Winston, Dominion Diamonds and Gem Diamonds.

JPMorgan Chase and HSBC reportedly unwittingly processed payments for Wagner warlord Prigozhin

bne IntelliNews

Leading western banks JPMorgan Chase and HSBC unwittingly processed payments for companies linked to Russian warlord Yevgeny Prigozhin, the late leader of the Wagner Group Private Military Company, the *Financial Times* reported on September 24.

The payments were connected to Wagner's extensive operations in Africa where Prigozhin hired out Wagner's services to multiple regimes, earning billions of dollars in the process.

Prigozhin died last August when his private jet crashed outside Moscow in mysterious circumstances, shortly after he organised a march on Moscow in a military rebellion against Putin's regime, briefly capturing the southern city of Rostov.

Wagner has been accused of multiple human rights abuses in Africa where it acts as trainers or paramilitary support for various regimes. Leaked documents obtained by the Center for Advanced Defence Studies (C4ADS), a Washington-based think-tank, show how payments for companies controlled by Prigozhin flowed through major financial institutions as Wagner's operations expanded across the continent, the *FT* reports.

In 2017, Meroe Gold, a Sudanese company serving as a front for Wagner, purchased industrial equipment from China, with payments transiting via large Western banks. These transactions occurred before Meroe Gold was subject to sanctions, though Prigozhin himself had been sanctioned by the US in 2016.

Wagner often accepted payment in the form of mining concessions, including gold mines, and other business activity in the raw materials sectors from the mineral-rich, but cash-poor regimes in Africa. A search of Prigozhin's residence after his death found suitcases packed with millions of dollars of cash and gold bars amongst other things.

The Kremlin was happy to allow Wagner to operate in Africa as a tool of its foreign policy to bind African states closer to Moscow and as a counter to the US and French military presence in Africa. Wagner also played a crucial role in the Ukraine war, especially in the eight-month long siege and eventual capture of the city of Bakhmut.

Wagner's operations, according to the US Treasury, were notorious for "mass executions, rape, child abductions, and other brutalities against innocents" in Africa. Prigozhin was also well known for recruiting Russian prisoners, offering them a pardon for six months of service, but using them as cannon fodder on the battlefield.

Amongst the leaked documents, one invoice from August 2017 reveals that Meroe Gold used a local Sudanese bank account to send a payment via JPMorgan Chase in New York to a Chinese supplier, the *FT* reports. Another payment, processed through Hang Seng Bank – part of the HSBC Group – facilitated the purchase of diesel generators and spare parts. There is no indication that the banks involved were aware they were handling transactions tied to Wagner front companies.

Although Meroe Gold was not under sanctions at the time, it was later targeted by the US in 2018 for being "owned or controlled by Prigozhin" and for helping him "exploit Sudan's natural resources for personal gain."

Both JPMorgan and HSBC distanced themselves from the revelations. JPMorgan stated: "After a review of the limited details shared with us, we have not found any records matching those transactions." HSBC declined to comment on the Sudanese payments specifically but reiterated its dedication to combating financial crime, stating it has "invested significantly in building and maintaining an effective control framework to detect and mitigate this risk."

C4ADS stated that the transactions demonstrate Wagner's ability to blur the lines between licit and illicit activity. "To facilitate its early exploitation of natural resources, the internationally sanctioned organisation relied on a network of financial services and transportation networks to move supplies and generate revenue," C4ADS said in its report.

Following Prigozhin's death Wagner's African operations have reportedly been absorbed into entities controlled directly by Russia's defence ministry. Many of Wagner's leaders have joined the Armed Forces of Russia (AFR) and have been credited with bringing fresh and more effective tactics to Russia's military operations in the current operations to take the key Ukrainian city of Pokrovsk.

Since US President Joe Biden signed an executive order in December, new so-called strangulation sanctions have been effectively targeting Russian banking operations making payments to Russian entities via third party banks more difficult.

Wagner operated in numerous African countries including:

Central African Republic (CAR): Wagner was heavily involved in CAR, providing security services to President Faustin-Archange Touadéra's government in exchange for access to diamond and gold mining rights. They were also reported to have protected government officials and trained local forces.

Sudan: Wagner had a significant presence in Sudan, where it supported the government of former President Omar al-Bashir. Wagner's operations involved providing military training and securing mining concessions, particularly for gold. After Bashir's ousting, the group reportedly maintained influence with Sudan's military leadership.

Libya: Wagner played a prominent role in the Libyan civil war, backing the forces of General Khalifa Haftar's Libyan National Army (LNA) against the UN-recognised Government of National Accord (GNA). Wagner fighters were reportedly deployed to support Haftar's offensive on Tripoli.

Mali: Wagner expanded its operations in Mali after the country's military coup in 2020, forming close ties with the junta. The Malian government hired Wagner mercenaries under the guise of combating terrorism, but their presence also coincided with growing instability and reports of human rights abuses.

Mozambique: Wagner was involved in combating Islamist insurgents in northern Mozambique, particularly in the Cabo Delgado region, which is rich in natural gas. However, the group reportedly faced setbacks, with several fighters killed and operations scaled back.

Madagascar: Wagner provided political and security consultancy services during the 2018 presidential elections in Madagascar, reportedly supporting President Andry Rajoelina's campaign.

Burkina Faso: There are indications that Wagner has been increasing its influence in Burkina Faso, particularly following the military coups in 2022 and 2023, where the junta sought external security support amid rising jihadist violence. ●

Fast fashion slowly conquers the Balkans

Shoppers queue for the opening of Albania's first H&M store.

Clare Nuttall in Glasgow

Six years ago, *bne IntelliNews* explored the spread of fast fashion into new frontiers, highlighting how major Western fashion retailers like Inditex and H&M had largely focused on larger emerging markets, with the number of stores broadly correlating to the GDP of each country. At the time, only Romania, Southeast Europe's largest economy, saw significant penetration from these fashion giants.

Today, while the Balkan markets remain small, international fashion chains are steadily gaining ground, with several new store openings in recent years. However, this expansion has been inconsistent, driven not only by the size or overall attractiveness of the economies, but also by the ability to work with reliable local partners and secure space in modern shopping malls. This is particularly evident in smaller countries such as Kosovo and North Macedonia.

The rise of fast fashion

Fast fashion refers to retailers like H&M, Zara, Primark, and others that have revolutionised the industry in recent decades by slashing the time it takes to move from design to store shelves. Previously, this process took months, but fast fashion companies condensed it to just weeks, producing low-cost garments in a variety of constantly changing styles. Between 2000 and 2014, the number of garments purchased in Western markets doubled, surpassing 100bn items annually.

Western fast fashion brands began entering Central and Eastern Europe in the early 2000s. Over the last two decades, they have expanded from Central Europe into the Balkans and further east into Russia and beyond. With feeding the demand for ever more clothes at the heart of their business model, these companies have been expanding geographically to sustain growth.

Expansion into emerging markets
By 2018, nearly half of Inditex's stores – the group includes Zara as well as brands such as Bull & Bear, Bershka and Stradivarius – were in emerging markets, while H&M had about 30% of its outlets in these regions. In Eastern Europe, the number of stores generally corresponded to GDP figures, meaning the largest markets like Poland, Romania, and Russia saw the most stores. However, smaller Balkan countries, along with Central Asia (except Kazakhstan), had a much smaller presence.

One exception was Italy's Teddy Group, the Italian parent company of Terranova. Terranova was an extremely early entrant into emerging Europe, picking newly independent Croatia as its second market for international expansion (after Spain) as early as December 1991. With Croatia already embroiled in what was to be a bloody four-year war, the first Terranova store opened in Zadar, in what one Teddy Group executive recalled was an "air of expectation and hope". Today, Terranova is active across the region, having aggressively ventured into frontier markets like Kosovo and Moldova, and plans to open 150 stores worldwide in 2024.

Romania the top market
Six years on, Inditex's main presence in the region, with 148 stores, was clearly Romania, which has by far the biggest economy and largest population. Inditex also had dozens of stores in some of the other larger economies – Croatia, Bulgaria and Serbia. There were fewer stores in the smaller markets such as Albania, Montenegro and North Macedonia, and none at all in Kosovo or Moldova.

Similarly H&M had 53 stores in Romania, between 10 and 20 each in Bulgaria, Croatia, Serbia and Slovenia, just a handful in the smaller markets. Indeed, H&M only recently entered Bosnia (in 2019), North Macedonia (in 2022) and Albania the following year, opting for Balfin Group's East Gate Malls in both Skopje and Tirana. Zara and other brands from Inditex's portfolio are also present at the Skopje East Gate Mall, alongside the first brands from Poland's LLP to enter the country.

Primark, another Western fast fashion retailer, was relatively late. It made its entrance into Southeast Europe in 2019, opting to open first store in the region in tiny though prosperous Slovenia. It has since expanded to Romania and other emerging European markets.

Turkish competition
As Western retailers moved east, they encountered stiff competition from Turkish fast fashion chains like Koton and LC Waikiki, which were early movers into several emerging markets, particularly those with cultural or historical ties to Turkey. LC Waikiki's appeal in majority Muslim countries, with its modest clothing options, gave it a distinct advantage in markets like the Balkans.

While Koton and LC Waikiki struggled in more affluent Western European markets due to higher costs and intense competition, they secured strong positions in Southeast Europe and Eurasia.

Looking at the LC Waikiki stores in Southeast Europe, the retailer has 45 in Romania, but 32 in Bosnia – a market less than one tenth of the size.

Post-communist retail transformation
The arrival of Western fast fashion was just the latest chapter in the retail evolution of post-communist Eastern Europe and Eurasia. Following the fall of communism, the region experienced a flood of cheap imports from China and Turkey, often brought in by small traders. Eventually, large wholesale bazaars dominated the landscape. Before modern malls and brand-name stores arrived, wealthier Eastern Europeans would fly to Western capitals to shop, while the majority of consumers struggled to keep up with Western fashion trends.

Today, international brands have become ubiquitous in the region's EU member states and are making headway in the Western Balkans. As incomes rise, these markets are becoming more attractive to global retailers.

Recent geopolitical shifts have also had an impact. In the wake of Russia's invasion of Ukraine, many Western retailers pulled out of the Russian market, which had been a key focus for companies like H&M and Inditex. Both brands closed hundreds of stores in Russia, transferring some to other operators.

"Today, international brands have become ubiquitous in the region's EU member states and are making headway in the Western Balkans. As incomes rise, these markets are becoming more attractive to global retailers"

As brick-and-mortar stores continue to expand across the Balkans and Eurasia, online retailers are also making inroads. The pandemic accelerated this trend, with Chinese giants like Shein, Temu and Aliexpress aggressively expanding their presence in emerging markets. Emerging Europe also has a homegrown online retail champion; Lithuania-born second-hand marketplace Vinted.

Accordingly, fast fashion, both online and in stores, continues to evolve, and is increasingly shaping the retail landscape in the Balkans. ●

bne:Funds

Poland's Zabka Group IPO could make it Warsaw's new blue chip

Wojciech Kosc in Warsaw

Poland's convenience store chain Zabka Group has announced plans for an initial public offering (IPO) and listing on the Warsaw Stock Exchange, the company's main shareholder, the investment fund CVC, said on September 23.

Details or the timeline for the offering were not disclosed other than the target will be international institutional investors and individual investors in Poland.

The offering could be worth between PLN4bn - PLN6bn (€780mn - €1.18bn), which would put the company's overall valuation estimated at PLN30bn - PLN32bn, *Bloomberg* reported in June.

"However, unofficial reports suggest the offering could be much larger, potentially reaching several billion, which would increase Zabka's chances of quickly joining the [GPW's blue-chip] WIG20 index," the newspaper Puls Biznesu reported.

"The IPO will allow selling shareholders to partially realise their investment in Zabka Group. Additionally, the management believes the IPO will provide improved access to domestic and international capital markets should there be a need to raise funds in the future, particularly for financing potential mergers and acquisitions," CVC said in a statement.

Zabka's revenues grew 24% to PLN19.8bn in 2023, with like-for-like (LFL) sales increasing 10.8%. The group's adjusted Ebitda rose 17% to PLN2.83bn.

In the first half of 2024, revenues increased 21.5% y/y to PLN11.1bn, with LFL sales up 10.3%. Adjusted Ebitda surged 33.5% to PLN1.4bn.

For the third quarter, Zabka expects LFL growth in the upper range of mid-single digits, partly due to a high base effect and favourable weather in Q3 2023. For the full year 2024, the company anticipates high single-digit LFL growth of 7.5%-9%.

Zabka's goal is to improve its adjusted Ebitda margin, aiming for the upper end of the 12%-13% range in the medium term. The company also expects margin growth to accelerate in the short term, supported by stabilising energy prices and growing economies of scale.

In 2024, Zabka plans to open around 1,100 new stores, and in the medium term, it aims to open over 1,000 stores annually in Poland and Romania. ●

The IPO could value the company at PLN30bn - PLN32bn (euro7bn-7.5bn) / Cybularny

Rising gold ETF inflows set to drive global bullion prices

gold / Pexels - Michael Steinberg

bno - Mumbai Office

Inflows into gold exchange-traded funds (ETFs), particularly from Western investors, are expected to increase in the coming months, adding more upward momentum to already record-high bullion prices, analysts have said, according to a *Reuters* report.

Gold prices have risen by 27% this year, reaching $2,600 per ounce, primarily driven by looser central bank monetary policies and geopolitical tensions. Recent interest rate cuts in the US, Europe, and China have fuelled optimism for further gains, with expectations that gold prices could reach a new high of $3,000.

"Exchange-traded products (ETPs), or ETFs, allow investors to gain exposure to gold without physically holding the metal"

Exchange-traded products (ETPs), or ETFs, allow investors to gain exposure to gold without physically holding the metal. Any increase in ETP holdings is significant for prices, as these funds are backed by the physical commodity. A rise in inflows will reduce the available supply of gold on the market, further boosting prices.

Analysts at Standard Chartered expect inflows into ETPs to accelerate now that central banks have begun cutting interest rates, Reuters said. This will likely support the next phase of gold's price rally. ETP flows, which tend to correlate with real yields and the value of the dollar, have turned positive. While Europe initially drove most of the inflows, North America has seen a resurgence of interest over the past two months, the news agency added.

According to the World Gold Council (WGC), global gold ETFs recorded inflows of 28.5 tonnes, or $2.1bn, in August, with all regions contributing positively. Western funds accounted for the largest share, with North America adding 17.2 tonnes, or $1.4bn, in the same month. Softer US economic data, dovish Federal Reserve comments, a weaker dollar, and lower yields helped drive these inflows, according to the WGC.

Major financial institutions, such as J.P. Morgan, Goldman Sachs, Citi, and UBS, have reiterated their bullish outlook on gold, predicting further price increases as ETF holdings grow. Goldman Sachs noted that the Federal Reserve's rate cuts are expected to attract Western capital back into gold ETFs, a factor that has been largely absent from the gold rally in the past two years, *Reuters* reported.

J.P. Morgan also highlighted that retail-focused ETF inflows will be crucial for sustaining the ongoing gold rally and has projected a peak price of $2,850 by 2025.

Spot gold recently hit a record high of $2,639.95 per ounce, driven by expectations of further monetary easing and geopolitical concerns. Lower interest rates reduce the opportunity cost of holding non-yielding assets like gold, which is seen as a safe haven during periods of market instability.

Ole Hansen, head of commodity strategy at Saxo Bank, noted that while falling interest rates have underpinned the surge in ETF demand, it remains to be seen whether investors are willing to buy gold at such elevated prices. ●

"Major financial institutions, such as J.P. Morgan, Goldman Sachs, Citi, and UBS, have reiterated their bullish outlook on gold, predicting further price increases as ETF holdings grow"

bne:Bond

Ukraine's bondholders sign off on $20bn debt restructuring deal

bne IntelliNews

Ukraine's bondholders formally signed off on September 3 on the deal for restructuring $20bn of debt, which will result in repayments being suspended for several years and will take the pressure off the cash-strapped government.

Kyiv has confirmed that holders of over 97% of its debt agreed to the restructuring plan by the required deadline, allowing the process to move forward. The deal is set to reduce the face value of Ukraine's international bonds by $11.4bn, or more than a third, over the next three years.

Doing the deal was a key condition set by the International Monetary Fund (IMF) to ensure the country's debt remains sustainable. An IMF team is due in Kyiv this week to discuss the conditions for releasing the next tranche of Ukraine's Extended Fund Facility (EFF) support worth billions of dollars.

While Ukraine's ability to return to international capital markets hinges on the end of the war with Russia, finalising the restructuring represents a "crucial step" for the country ahead of the eventual reconstruction when Ukraine will have to raise billions of dollars from private investors, according to Finance Minister Serhiy Marchenko. He said that the agreement would "ensure Ukraine maintains the budget stability needed to continue financing our defence" and is pivotal in restoring long-term economic stability.

Bondholders had granted a two-year payment suspension in 2022 after the onset of the conflict, but Ukraine found this insufficient, requiring a major bond debt restructuring this year to maintain the flow of IMF loans. The restructuring will reduce the cost of the debt by approximately 60%, with Ukraine resuming interest payments at a significantly lower rate after the suspension, which officially expired in August, *UBN* reports.

The deal will involve bondholders writing off 37% of their claims, with the debt write-off potentially decreasing to 25% if Ukraine's GDP exceeds IMF targets set for 2028.

Bondholders will receive new bonds worth 40 cents on the dollar of their original holding, with interest payments restarting immediately. The payments are scheduled to start at 1.75%, rising to 4.5% in 2026, 6% in 2027, and reaching 7.75% from 2034 onwards.

Additionally, bondholders will receive a second bond series worth 23 cents on the dollar, which will not pay interest until August 2027. However, this bond's value could increase to 35 cents if Ukraine's economy outperforms IMF targets by at least 3% by 2028. The new bonds are expected to start trading on 30 August, once the final details of the restructuring are settled.

Kyiv has confirmed that holders of over 97% of its debt agreed to the restructuring plan by the required deadline, allowing the process to move forward.

The newly agreed restructuring only covers Ukraine's international market bonds, which account for $24bn, or approximately 15% of the country's total debt, which exceeds $140bn.

Additionally, Ukraine still needs to negotiate a separate restructuring deal in the coming months of $2.6bn in GDP warrants issued during the 2015 restructuring and that were just starting to pay out to investors before the war started.

Real challenges may arise in 2027 when Ukraine's official creditors will need to restructure their own debts at the end of the current IMF programme. Kyiv is expected to record a deficit of $43bn this year to cover high military expenditures amid delays in Western aid earlier this year.

Government short of cash

The government is already running short of money as there is a $12bn hole in the budget due to increased military spending and the government is mulling raising taxes and cutting non-essential spending to cover the shortfall. Ukraine will also need to cover a budget deficit of $35bn next year. The Ministry of Finance (MinFin) has also said there is a $15bn hole in the 2025 budget forecast too, due to dwindling international support.

In August, the state budget's general fund received about $8.4bn in external financing. As noted by the Ministry of Finance, $5.5bn comprised grants (65%), and $2.9bn arrived through preferential financing. This includes $4.5bn in concessional financing and a grant from the EU and a $3.9bn grant from the US.

The funds from the EU are the first regular tranche (provided upon fulfilment of conditions) within the framework of the Ukraine Facility. The financing consists of a $2.9bn loan and a $1.6bn grant.

Kyiv received the grant from Washington through the World Bank's Peace in Ukraine project. The funds are to be used for salaries of teachers, emergency responders, civil servants and social expenses. In total, this year Ukraine has already received $24.5bn in external funding, including $6.6bn in grants.

In addition, in August the state budget's general fund received UAH386.2bn ($9.4bn) in taxes, fees and payments. This is 200% more than in July.

Last-minute deal

This restructuring is the second Ukraine has been forced to undertake in a decade following Russian military aggression. The previous restructuring occurred in 2015 after Russia's annexation of Crimea. The current process required the backing of at least two-thirds of Ukraine's bondholders, along with a simple majority in each of the individual bond series involved.

The negotiations, which took only four months, proceeded at an unprecedented pace, replacing a two-year bond payment moratorium granted to Ukraine in the summer of 2022, now nearing expiration.

Yuriy Butsa, head of Ukraine's debt agency and a central figure in the negotiations, remarked on the unique nature of this restructuring. "This has not been driven by any unsustainable economic policies," Butsa told *Reuters*. "It is driven solely by the Russian aggression against Ukraine," adding that the process had been one of the quickest debt restructurings in history.

The Group of Creditors of Ukraine, comprising the country's bilateral lenders, including Canada, France, Germany, Japan, the United Kingdom and the United States, welcomed the agreement.

"The swift implementation of the exchange demonstrates substantive support for the government and people of Ukraine by providing substantial debt relief," the group told *Euroactiv*. ●

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bne:Tech

Nebius enters European AI infrastructure race with multi-billion-dollar investment plan

Vladimir Kozlov in Cyprus

Nebius, an AI firm formed as a result of a spinoff of Russian IT giant Yandex' international business, has announced the launch of a new GPU cluster in Paris. The move comes as part of the company's plans to invest more than $1bn by mid-2025 in AI infrastructure in Europe.

"We work in a new industry which requires both deep technology and significant capital," Arkady Volozh, founder and CEO of Nebius, said in a statement shared with *bne IntelliNews*.

"Our data centre in Finland already provides the latest high-performance compute, tools and services to AI developers around the world. The addition of our new GPU cluster in Paris is the next step in our plan to expand Europe's AI capacity as we develop Nebius into a leading global AI infrastructure company," he added.

Nebius is launching a new GPU cluster in Paris, becoming one of the first in Europe to offer NVIDIA's H200 Tensor Core GPUs. As an NVIDIA cloud and OEM partner, Nebius will also be among the first to provide customers with the cutting-edge Blackwell platform in 2025. Already a leading GPU capacity provider in Europe, particularly through its energy-efficient data centre in Mäntsälä, Finland, Nebius is expanding its AI infrastructure through investments in new greenfield data centres and increased capacity at existing locations.

The company has signed agreements to construct two new data centres in Europe and is already working on expanding its Finnish facility. These initiatives, which include roughly $200mn in investments since early this year, will enable Nebius to support tens of thousands of GPUs, enhancing its AI cloud services globally. Built to meet the growing demands of the AI industry, Nebius draws on deep technical expertise in hardware, software, and machine learning. Its team of over 500 engineers brings decades of experience in building top-tier tech infrastructure, supported by an in-house LLM R&D team.

Earlier this year, the split of Yandex, often referred to as the "Russian Google, was completed, and the Russian tech behemoth's former international business was renamed Nebius Group, which consists of four firms: Nebius AI, Toloka AI, TripleTen, and Avride.

In July 2024, a group of Russian buyers completed a $5.4bn deal involving cash and shares to acquire Yandex's Russian operations. This marked the largest corporate exit since Russia's invasion of Ukraine in February 2022, though the transaction was made at a significant discount.

At that time, Nebius Group had a valuation of $2.11bn according to back of the envelope estimate conducted by analysts at Seeking Alpha.

Arkady Volozh, founder and CEO of Nebius, says that the firm is entering into the global technology race with an investment of over $1bn into AI this year.

Nebius AI is focused on building full-stack infrastructure to service the explosive growth of the global AI industry, including large-scale GPU clusters, cloud platforms, and tools and services for developers. Headquartered in Amsterdam and listed on Nasdaq, the company has a global footprint with R&D hubs across Europe, North America and Israel.

Nebius's core business is an AI-centric cloud platform built for intensive AI workloads. With proprietary cloud software architecture and hardware designed in-house (including servers, racks and data centre design), Nebius gives AI builders the compute, storage, managed services and tools they need to build, tune and run their models.

An NVIDIA preferred cloud service provider, Nebius offers high-end infrastructure optimized for AI training and inference. The company boasts a team of over 500 skilled engineers, delivering a true hyperscale cloud experience tailored for AI builders. ●

Albania plans AI-driven public procurement

Aida Kadyrzhanova in Prague

Albania has plans to build a new, fully transparent and 95% AI-based model for public procurement, as stated by Prime Minister Edi Rama during his address at the 79th session of the United Nations General Assembly.

In his speech on "Dialogue for the Digital Future", Rama highlighted the benefits of digital technology for developing countries.

The Albanian government took most public services including tax payment online via the e-Albania portal as of May 1, 2022 while in-person service windows in government offices and other institutions were shut down.

Rama noted that the transition to offering 95% of services online has eliminated long queues at government offices. He explained that the government is using artificial intelligence to accelerate its European Union membership negotiations.

However, he also addressed the risks associated with technology, citing a recent cyberattack on Albania linked to Iran.

Albania's cybersecurity authorities attributed the attack on the Institute of Statistics in February to a hacker group allegedly supported by the Iranian government. The Institute reported a sophisticated cyberattack on February 1, which affected multiple systems and 40 computers.

“We have seen how technology can harm countries and citizens, but by maximising its benefits while curbing its misuse, we can create a better world,” Rama concluded.●

Serbia hikes ICT exports as Russian tech professionals boost sector

Tatyana Kekic in Belgrade

Serbia’s total exports of ICT services for January to July 2024 reached €2.306bn, which is a 20% increase compared to the same period in 2023, according to the National Bank of Serbia (NBS).

The country’s ICT sector has witnessed remarkable growth over the past decade. In 2012 ICT service exports were valued at €375mn; by 2023 this figure had grown almost tenfold to €3.44bn.

Data from the NBS highlights a particularly strong performance in July 2024, where ICT service exports alone amounted to €362mn, marking a 29% increase compared to July 2023. The surplus for the first seven months of 2024 in ICT services stood at €1.787bn, underscoring the sector’s profitability and export potential.

Serbia has a solid engineering tradition of its own, but the influx of tens of thousands of Russian professionals since the start of the Russia-Ukraine war has significantly bolstered the local ICT sector.

It is estimated that around 300,000 Russians have come to Serbia since February 2022, and that as many as 50,000 have obtained residence permits. A large number are highly skilled and work in the IT sector or consulting.

Industry experts anticipate that the upward trend in Serbia's ICT sector will continue, driven by both domestic talent and the inflow of international expertise. ●

China leads the world in wind power generation both in terms of installed capacity and the rate at which it is adding more capacity, according to the World Energy 2024 report. / bne IntelliNews

bne:Green

Global wind power installations reached a new high in 2023

bne IntelliNews

Global wind power installations reached a new high in 2023, increasing renewable energy's share of total power generation to 30%. Who are the leading countries?

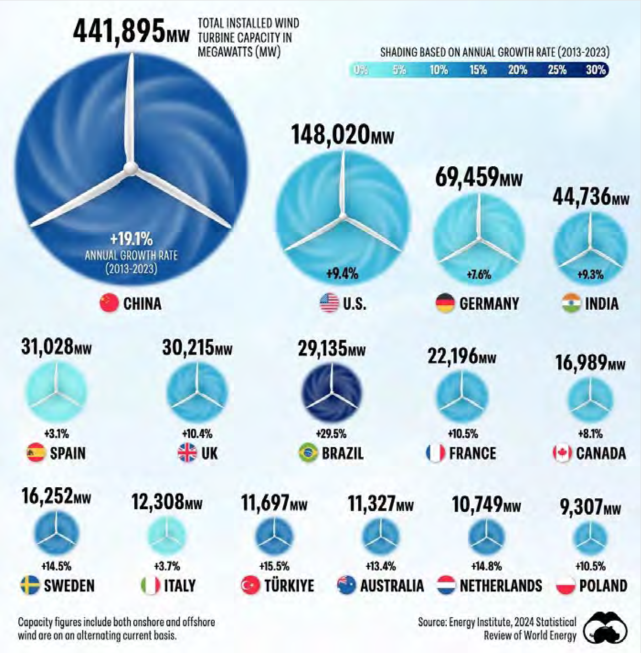
China leads the top 15 countries by total installed wind turbine capacity with 442GW and the growth rate of new capacity is running at 19.1% per year, based on data from the Energy Institute's Statistical Review of World Energy 2024 report.

The US is in second place with 148GW, with a much more modest growth rate of 9.4%. Germany leads Europe with 68GW and a 7.6% growth rate. And India is in fourth place with 45GW and a growth rate of 9.3%.

In 2023, clean power made up 35% of China's electricity mix, with hydro the largest single source of clean power at 13%. Wind and solar hit a new record share of 16%, above the global average (13%). China generated 37% of global wind and solar electricity in 2023, enough to power Japan.

Renewables make up 24% of US energy generation but that is expected to rise to 26% by the end of this year, according to International Energy Agency (IEA): natural gas accounts for

Wind Installations as of 2023



31.8%; petroleum (crude oil and natural gas plant liquids) for 28%; and coal for 17.8%.

Germany has one of the highest shares of renewables in its energy mix of any major economy: 57.1% in 2023, compared to 50.2% in 2022.

While India remains heavily dependent on coal to meet its economy's insatiable appetite for energy to fuel its fast economic growth, renewable sources accounted for 19.5% of India's electricity generation in 2023, up from 15.2% in 2010.

India is anticipated to meet its targets of a 50% non-fossil fuel energy share and a renewable energy capacity of 500GW before 2030.

While China and India remain amongst the biggest emitters of greenhouse gases (GHGs), they both have ample reserves in their carbon budget – the amount of permissible emissions under the terms of the 2015 Paris Agreement – as they transition to a green economy. The West, however, has long since used up its carbon budget allocation and is now in carbon debt. China remains the global green energy champion and has already reportedly passed peak emissions, whereas thanks to the growing use of fossil fuels amongst the Western economies, emissions have reached an all-time high and are continuing to climb. ●

Infrastructure bottleneck could thwart Kazakhstan's ambition to export green hydrogen to Europe

A space shuttle main engine burning hydrogen with oxygen, produces a nearly invisible flame at full thrust. / Nasa, public domain

bne IntelliNews

Kazakhstan's ambitions in producing and exporting green hydrogen to the EU may never come to fruition because of infrastructure, logistical hurdles and other challenges but the Central Asian country should look hard at using the clean commodity in producing higher-value green industrial products both for domestic use and export, according to an analytical article published by Carnegie Endowment's Carnegie Politika think tank.

The EU and Kazakhstan in November 2022 signed a strategic partnership on the production of green hydrogen (hydrogen produced by the electrolysis of water powered by renewable electricity) and critical raw materials (CRM) and in March 2023, Germany opened a Hydrogen Diplomacy Office in Astana.

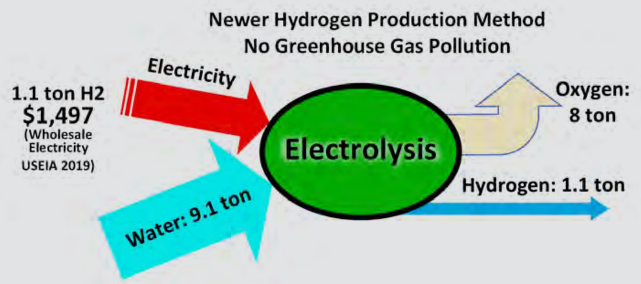
In her article, Yana Zabanova, a PhD candidate at the University of Groningen and research associate at the Research Institute for Sustainability, Helmholtz Centre Potsdam (RIFS Potsdam), focuses on developments that have occurred since the partnership was sealed amid the EU's plans to import up to 10mn tonnes of green hydrogen by 2030 and various challenges Europe has so far faced in achieving this goal.

For Europe, cross-border hydrogen infrastructure has remained expensive (and the EU has a very limited budget to finance such infrastructure links with third countries), the pace of hydrogen cost reductions has been slower than anticipated and demand from industry for clean hydrogen has been weaker than expected. In July, the European Court of Auditors highlighted these issues and called for a "reality check" as regards the European bloc's hydrogen policy, raising doubts about the production and import targets.

Geoeconomics and geopolitics analyst Zabanova argues that for potential producers like Kazakhstan, the current situation with the infrastructure bottleneck and other difficulties raises the question of whether they should focus more on using hydrogen to decarbonise their domestic economies rather than prioritising exports.

"Challenges such as the high cost and lack of transport infrastructure are significant obstacles to exporting hydrogen from Kazakhstan to Europe"

Kazakhstan's hydrogen potential first gained international attention in June 2021, when Swedish-German energy company Svevind announced a $50bn green hydrogen project in the country. Known as HyrasiaOne, this project aims to install 40 gigawatts of wind and solar capacity in the Mangystau region near the Caspian Sea to produce 2mn tonnes of green hydrogen or 11mn tonnes of green ammonia by 2030. Despite some scepticism about feasibility, an official investment agreement was signed with the Kazakh government in October 2022, and the project is now in its conceptual engineering phase. A final investment decision is expected by 2026.



Green hydrogen is produced by the electrolysis of water powered by renewable electricity (Credit: Parent55, cc-by-sa 1.0).

The potential for exporting hydrogen to Europe has been a key factor in attracting investors like Svevind to Kazakhstan. However, challenges such as the high cost and lack of transport infrastructure are significant obstacles to exporting hydrogen from Kazakhstan to Europe, Zabanova writes.

Moreover, uncertainties remain regarding the scale and timeline of upcoming EU hydrogen demand. While the EU has set binding quotas for green hydrogen use in industry and transport that kick in in 2030, initial demand may largely be met by European suppliers, the analyst says. Although Germany is a strong advocate for hydrogen trade, other EU member states prefer to focus on domestic production.

"Prior to the war in Ukraine, it might have been conceivable to transport Kazakh hydrogen to Europe through Russian territory via retrofitted gas pipelines," Zabanova notes. "But that is no longer a palatable option, and the alternatives are complicated. One possibility would be to construct an offshore hydrogen pipeline crossing the Caspian Sea and continuing to Southern Europe through the Caucasus and Turkey. However, Russia has strongly opposed the construction of any trans-Caspian pipelines in the past and would likely raise objections on environmental grounds this time as well."

Zabanova believes that the export of clean hydrogen is not Kazakhstan's only opportunity when it comes to the green commodity. Increasing global interest in using clean hydrogen to produce higher-value industrial products – such as green fertilisers, steel and e-fuels – both for the domestic market and export customers offers a promising avenue for the country, she says.

This approach aligns with recommendations from the Central Asian & European Hydrogen Diplomacy Forum held in Astana in May 2024, which sees potential for hydrogen to decarbonise Kazakhstan's economy.

Projects like HyrasiaOne have indicated a willingness to supply the domestic market, potentially decarbonising industries such as refineries, steel production and chemicals, though that would require substantial investment, the analyst posits.

"Kazakhstan could use green hydrogen to decarbonize its refineries, steel production, and the chemical industry, although that would require significant levels of new investment," Zabanova says. "So far, only Kazakhstan's national oil and gas company KazMunayGas (KMG) has made tentative steps in this direction. In 2022, its subsidiary KMG Engineering launched the Hydrogen Energy Competence Center and the Hydrogen Technologies Research Laboratory in Atyrau. KMG is currently planning pilot clean hydrogen projects as part of its low-carbon development strategy."

Neighbouring Uzbekistan's efforts to produce green ammonia with Saudi Arabia's ACWA Power provide an example Kazakhstan could follow, according to Zabanova.

Despite the potential, Kazakhstan currently lacks a developed hydrogen policy framework. Although the country's 2060 Net Zero Strategy references hydrogen for decarbonisation, there are no specific targets or policy instruments to stimulate hydrogen demand.

"While the concept sets ambitious targets, including 10 gigawatts in electrolyser capacity and 10 gigawatts of renewable generation capacity, it lacks clear priorities and remains largely aspirational"

The only progress worthy of note was the April 2024 draft Hydrogen Development Concept for 2040 published by Kazakhstan's Energy Ministry. It prioritises economic diversification, R&D and a pilot blue hydrogen project by 2030.

While the concept sets ambitious targets, including 10 gigawatts in electrolyser capacity and 10 gigawatts of renewable generation capacity, it lacks clear priorities and remains largely aspirational, Zabanova concludes.

Only time will tell whether Kazakhstan's hydrogen ambitions have realistic prospects. ●

EUROPE HAS LOST ITS COMPETITIVE EDGE

Ben Aris in Berlin

In the first year of the war in Ukraine the lights started to go out across Europe as the consequences of cutting off Russian trade and gas began to kick in. The end of cheap Russian energy imports was disastrous, causing an energy crisis that quickly spilled over into Europe's economy as the biggest chemical and metallurgical plants ceased to be economically viable and were shuttered. "De-industrialisation" has become the buzzword but Europe's problems run deeper than the economic shock caused by the war and were well entrenched long before Russian President Vladimir Putin ordered the invasion of Ukraine. Europe had already lost its competitive edge.

Two and half years on and the energy crisis has receded but not the de-industrialisation. Indeed, sanctions on Russia have catalysed the other problems and made them more visible. Sanctions are doing as much damage to the EU as they do to Russia, or more.

Europe became bloated on cheap energy, but innovation was stifled by reams of Brussels's red tape. The Union is half baked with federated trade and monetary policy, but the administration of regulations and fiscal policy remain under the control of national governments. The need for unanimity on all EU legal decisions works well in quiet times, but has proved cumbersome in times of crisis.

A year ago European Commission President Ursula von der Leyen commissioned former Italian Prime Minister and ex-European Central Bank boss Mario Draghi to compile a report on Europe's competitiveness, which was released in September.

And its conclusions have been a bombshell. Draghi outlines in detail the structural problems and shortcomings of the European system and says the EU now needs to invest more money to reinvent itself than it spent on repairing the damage from WWII.

The boomerang effect

Within days of the invasion of Ukraine on February 22, 2022, von der Leyen took to the podium and announced the most extreme set of sanctions ever imposed on another country. There have fourteen rounds since then, targeting everything that makes Russia money. The problem is that Russia used to make money from selling products and materials to Europe, inputs that are essential to European business.

As *bne IntelliNews* reported, the boomerang effect of the sanctions is weighing very heavily on Europe and comes on top of the polycrisis that included the global pandemic that had already knocked the EU for six. The one-time engine of Europe, Germany, is spluttering and has become the weakest economy in the G7. The sanctions have cost Russia a lot of money, and probably doom it to long-term stagnation, but it is currently flourishing and one of the fastest growing major economies in the world. Things are going so well that a new war middle class has emerged in Russia who are enjoying a period of unprecedented prosperity.

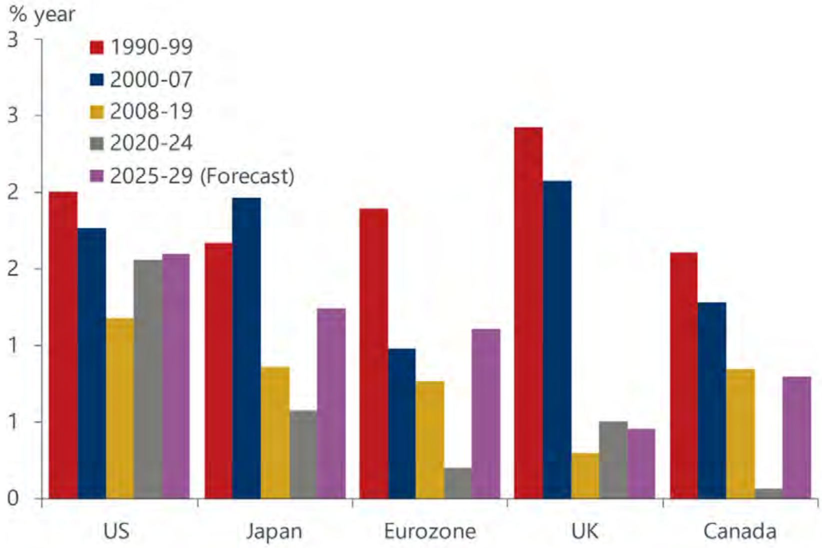
Europe had already fallen behind the US and the other G7 countries before the war started. It was feeling the growing pressure from the US and rising emerging markets before the war started. In 1995 European productivity was 95% of America's; today it is less than 80% and falling, says Draghi. The US and China continue to attract the bulk of global financing for tech frontiers that will fuel future growth, whereas Europe only gets the crumbs. That has already led to a European collapse in productivity over the last three decades.

"While the US productivity upturn is partly cyclical, it is also experiencing an underlying productivity renaissance. The country will continue to outperform most advanced economies, but we don't think much stronger GDP growth or far higher neutral rates are coming," Oxford Economics said in a note on September 20, adding that both the UK and the Eurozone have underperformed compared to their peers.

The developed nations can no longer compete with emerging markets in more complicated sectors as the combination lower wages, but rising skills, in medium- and heavy-weight industries has already made the developed world companies uncompetitive.

US manufacturing employment has fallen by a third from its peak in 1979, even as the population has grown by nearly 50% over the same period as the US also deindustrialises. Boeing and Intel are struggling; machine tools through industrial robots to consumer electronics are under increasing

Advanced economies: Hourly labour productivity



The hourly productivity of the EU has fallen behind that of most of the other major economies pressure. The list of American industries where manufacturing capability has been eroded is long.

Commercial shipbuilding in the US is particularly telling and now virtually non-existent. In 2022, the US had just five large oceangoing commercial ships on order, compared to China's 1,794 and South Korea's 734. The US Navy estimates that China's shipbuilding capacity is 232 times larger than in the US and it costs 2-4-times more to build a ship in the US than it does in the Global South, *Construction Physics* reports. The story is the same in the navies where China is building the equivalent of the entire French naval fleet every four years, but orders in Europe for new battleships are a fraction of those in the developing world.

Year End Orders for Large Oceangoing Ships

	2022	2021	2020
China	1794	626	441
South Korea	734	7,765	20.1
Japan	587	612	533
Europe	319	288	284
United States	5	3	4

Source: Brian Potter, Congressional Research Service

By contrast, as *bne IntelliNews* reported, China is the most powerful manufacturing country in the world, and, thanks to its industrial Soviet legacy, Russia is the manufacturer powerhouse in Europe, beating even Germany. Investment is now pouring into all these facilities as both Russian and China prepare for a possible global war.

Draghi has spent the last year studying the reasons for Europe's decline and released a 400-page report in September, "The future of European competitiveness", calling Europe to action.

De-industrialisation

Draghi's drill-down highlighted the ageing populations and the need to revamp defence and decarbonise economies. He especially highlighted the lag in technology. And he said all this need to be fixed just to keep growth standing still.

EU is sliding into a "slow agony" and is "ignoring obvious problems" according to the former Italian prime minister. On top of these structural problems, the lack of cheap resources from Russia adds salt to the wound.

The nature of the European economy has been fundamentally changed by the sanctions and the wholesale remake for global trade and energy markets, as Russia rapidly and successfully reoriented its oil trade from west to east. Over the last two years Putin has been remaking Russia's trade and diplomatic focus, cutting off Europe and rebuilding in the Global South. The balancing point in the cost-profit divide has slid dramatically to the cost end of the beam for Europe as a result. Energy prices have doubled and the prices of inputs and commodities across the board have increased. The chemical giant BASF has shuttered or reduced the output of hundreds of its European factories and 15% of German industrial companies have left the Continent and full half are saying they are considering the same option.

A miasma is hanging over European business, and industrialists see little prospect of a return to the status quo unless the sanctions on Russia are dropped and the gas is turned back on, according to *bne IntelliNews*' conversations with the members of the German industry lobby in Berlin.

But it is not just big business of heavy industry that has been affected; Germany is worst off as it is the most vulnerable to these changes. Manufacturing is the backbone of its economy and makes up around 20% of GDP – up to twice as high as the 10%-15% in countries such as France, Italy and Spain. Energy costs are now double their pre-war prices, thereby putting swathes of once profitable German export-orientated Mittlestand small- and medium-sized enterprises (SMEs) firms out of business.

Those that can are leaving the country in search of cheaper energy and labour homes. But they are less welcome than they used to be. China is tightening its grip as part of a fight for control over key resources in a slowly escalating tit-for-tat trade war. The West is responding to China's mounting challenge to Europe's long-standing lead in the automotive and renewables sectors by imposing trade tariffs to shield its increasingly flabby industries. Resource prices in Europe are 4-5 times higher than in the autarkic US, bureaucracy is more complex and taxes are exorbitant, says Draghi, putting further pressure on Europe's companies.

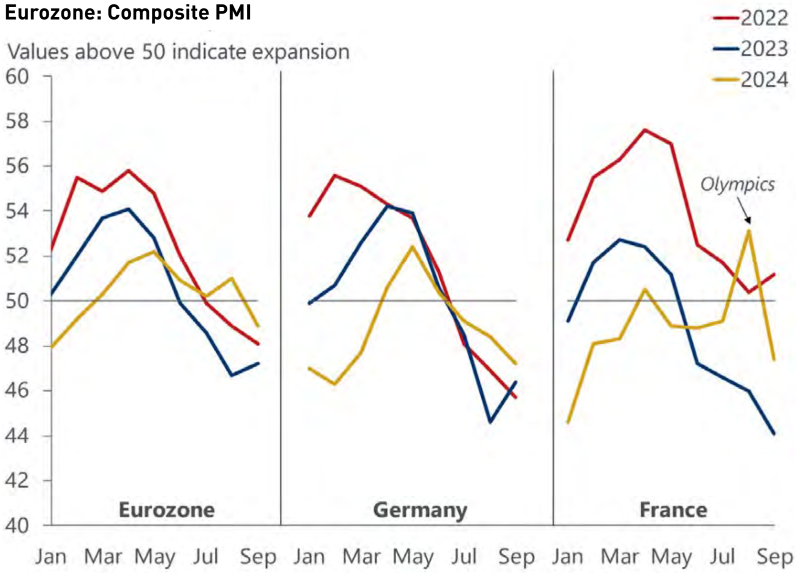
A miasma of despondency is descending on Europe as the scale of the challenge ahead becomes increasingly clear.

"Eurozone flash PMIs sank into contraction territory in September as the effect of the Paris Olympics faded, underlining the weak – and apparently deteriorating – economic conditions in the bloc. This was reinforced by another drop in Germany's ifo index and a still tepid credit flow to households and companies. The near-term outlook for the eurozone economy is bleak," Oxford Economics said in a note on September 27.

Draghi's solution is to throw money at the problem – massive amounts of money – and slash the red tape. He suggests annual investments of €800bn to stimulate EU industry over many years

"The nature of the European economy has been fundamentally changed by the sanctions and the wholesale remake for global trade and energy markets"

Eurozone: Composite PMI



September's Eurozone composite PMIs paint a bleak picture

Germany: Ifo business survey

German's falling IFO index shows economy is stuck in doldrums

– 5% of the EU's GDP and significantly higher than the 1-2% spent on post-World War II recovery. But even Draghi admits that change will not be fast.

It remains to be seen how long this new reality will last and if or when European economies can adjust to the new realities. In theory the revolution in clean energy could provide the cure for Germany's Russian gas addiction, but on this score the global green energy champion China is already way ahead of Europe – two thirds of all solar panels in existence are in China – which will reap the benefits of "free" energy long before Europe does. And the lack of minerals and other inputs in "deficit Europe" can never be solved. Europe has to turn to innovation and services as the only long-term option to retain its leading position, says Draghi.

"One reason why eurozone investment may have lagged is that it suffered from two major regional crises – the fiscal crisis in the early 2010s and, more recently, the Russian energy crisis. Accordingly, since 2010 there have been more reasons for eurozone firms to be cautious about the outlook for demand and, by extension, investing than their US counterparts. It is worth noting that crises tend to sap productivity as management is forced to spend less time innovating and more time 'fighting fires'," says Oxford Economics.

By contrast Russia is now investing heavily. The Kremlin has reversed its Putinomics, that effectively ran an austerity budget for the last decade, hoarding cash and paying down external debt while it built up the military, to pouring money into fixed investment and spending freely, especially on the military.

Businesses starting to downsize

The European deindustrialisation began with companies that directly bought Russian gas as a major input or used a lot of energy, representing about a tenth of Europe's GDP, but now the malaise is spreading further afield.

In September Germany's VW announced it will close plants in Germany for the first time in its 87-year history and is scaling back its EV ambitions. In a double whammy for Berlin, US chip-maker Intel has also decided to put plans for a new €30bn German gigafactory on ice and other new plants in Poland, Ireland, Spain, France and Italy. A question mark also hangs over a mooted Tesla gigafactory in Berlin as demand for the cars softens, but the company's gigafactory in Shanghai is going gangbusters.

The steel sector is also in trouble. Germany's steel industry employs about 80,000 workers, but most producers have reduced output due to high energy costs, a growing glut due to weakening Germany's car sales and falling machinery demand that is exacerbated by Russian sanctions, formerly a major client; pre-war machinery made up 45% of all Russia's imports, predominately from Germany. The story is the same in Germany's chemical industry, where a brief uptick faded away in August as the economy teeters on the edge of recession.

Nearly a third of major car plants from Europe's five largest automakers were underutilised last year. Stakes are high for EU economies: the automotive sector accounts for about 7% of EU GDP and more than 13mn jobs.

American brands Ford and General Motors, as well as Swedish Volvo, have found themselves in the same boat, announcing large-scale revisions of their plans to produce fully electric models in an effort to cut costs. In the US things have got so bad that in addition to a hefty import tariff, the Biden administration moved to completely ban all Chinese cars from the road with rules that "prohibit car manufacturers from selling cars in the US with important components or software from China", *The Guardian* reported on September 23.

“This effectively is the US admitting it is too weak to compete and retreating by shielding itself with protectionist rules under the guise of "national security". But paradoxically this will undoubtedly make it even weaker, as firms that are protected will have even less incentives to be competitive,” China watcher Arnaud Bertrand said in a post on social media.

German is not the only one that needs to pull its socks up. A revamped industrial policy is essential for the Central and Eastern European EU members (EU-CEE) if they are to escape the so-called "middle-income trap”, says a new report from the Vienna Institute for International Economic Studies (wiiw).

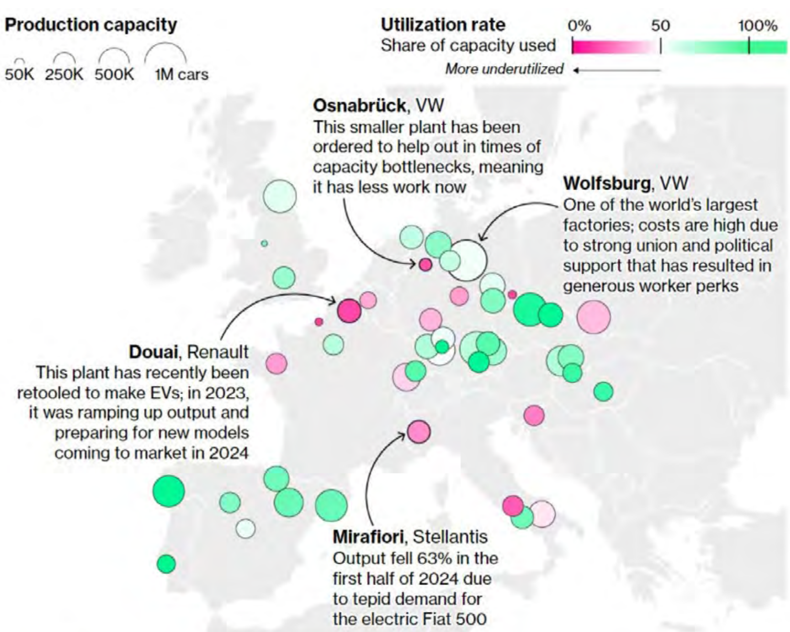
Having served as an "extended workbench" for Western firms by hosting labour-intensive production, the EU-CEE countries must now pivot toward innovation to maintain economic momentum. “The old model is exhausted,” wiiw says.

Like the rest of Europe, one of the key challenges facing EU-CEE countries is insufficient investment in research and development (R&D). While R&D expenditure is slowly rising, particularly in Poland, Czechia and Croatia, the region remains far behind the EU target of spending 3% of GDP on R&D.

“Above all, they are spending nowhere near enough money on research and development, which impairs their ability to innovate,” Zuzana Zavarská, economist at wiiw and co-author of the study, told *bne IntelliNews*.

A Third of Europe's Major Car Plants at Half Capacity or Less

Auto factories producing passenger vehicles for BMW, Mercedes, Renault, Stellantis and Volkswagen, 2023 data



Source: Bloomberg News analysis of Just Auto data
Note: A utilization rate of less than 50% is likely loss-making, according to Bloomberg Intelligence. Utilization rates of more than 100% can be achieved with overtime or by increasing the number of shifts. Plants that mostly produce commercial vehicles are excluded.

Only Slovenia and Czechia currently exceed 2% of GDP R&D expenditure, with other countries such as Slovakia, Bulgaria, Latvia and Romania spending less than 1%. Although some countries export medium- to high-tech products, much of this is driven by foreign multinational companies, and domestic firms struggle to benefit from advanced technological expertise.

In a rough comparison of unit costs in Germany against those of the US and China, and assuming that it takes one hour to make a widget out of one kilo of steel, using 5kWh of power, then assuming average 2023 industrial wages in Germany were €23.73 per hour, in the US the figure was \$18.31 and in China \$6; Germany’s unit cost for the widget is €26.73, the US’ \$20.16 and China’s \$7.55.

Defence and the peace dividend

Europe is at war with Russia, even if it doesn’t want to admit to it. The economic war began in the first week of the invasion, but as the Nato allies have scaled up their military support to Ukraine, this war has become increasingly classical and kinetic.

Europe has already dug deep into its stockpiles of weapons and ammunition and is now scrapping the barrel – a problem that is being made worse by the US’ increasing reluctance to supply Ukraine from its own extensive stockpile. New deliveries of things such as tanks or Patriot missile batteries, and especially F-16s, are all coming from Europe, not the US, despite the fact it maintains a huge surplus of nearly 1,000 planes vs the 72 in the EU. So far a total of only 10 F-16s have been sent to Ukraine, one of which was immediately destroyed.

Europe’s industry in general is under pressure, but the war has only highlighted the even more decrepit state of the European defence sector. It has atrophied after decades of sheltering under the US security umbrella through under-investment and preparing for the wrong war – the so-called “peace dividend.”

With a major war in its backyard and the real possibility of a Nato conflict with Russia, scarce resources are being channelled away into the defence sector where the spending needs run into the hundreds of billions of euros, not to mention the ongoing drain on the EU and national budgets for supporting Ukraine's war effort. Ukraine needs some €100bn a year of funding – two orders of magnitude more than the EU was providing pre-war – which is increasingly being funded by the EU, as the US starts to back off. Russia, on the other hand, has put its whole economy on a war footing, is massively outproducing Europe and is preparing to rebuild its military. Draghi included a whole section on modernising Europe's defence sector, which is a necessary security component to the economic prosperity plan.

"The world is heading into a period where foundational rules once taken for granted no longer apply. The EU urgently needs to emerge from its peace dividend softness and build a power model that allows it to shape new alliances and deter adversaries," political analyst Rym Momtaz wrote in a recent paper for Carnegie Endowment for International Peace entitled "Europe's Choice: Adapt or Atrophy."

As *bne IntelliNews* reported, the lack of investment in infrastructure and technology in business is mirrored by the chronic underinvestment in defence. Most of Europe is facing a serious materiel shortfall. Germany, in particular, will not be able to return to pre-war levels of armament for decades despite having earmarked a special €100bn in defence spending and formerly having one of the most powerful militaries on the Continent.

"Western Europe is at a particular disadvantage, having uniquely benefited, for nearly three generations, from a US-provided peace dividend, which exempted it from engaging in hard-power politics while allowing it to reap the rewards of global economic integration and cooperation," said Momtaz.

A clear example of Europe's military impotence was that in 2023 it promised to manufacture and deliver over 1mn shells to Ukraine by March this year. As *bne IntelliNews* reported, the EU has been very slow to sign military procurement contracts with weapons makers. The result: less than 200,000 shells were produced by the deadline. Currently Russia is firing ten shells for every one Ukrainian shell in Pokrovsk at the epicentre of the current battle. For comparison, Russia has raised its shell production from 1.7mn rounds a year in 2022 to 2mn last year. And it has sourced an additional million shells from allies such as North Korea.

"Russia's [military] is getting larger, and they're getting better than they were before. ... They are actually larger than they were when [the invasion] kicked off," Air Force General James Hecker told reporters at the Air & Space Forces Association's annual Air, Space & Cyber Conference on September 19.

Russia's military is now estimated to be 15% larger than it was at the start of the war, while Ukraine is suffering from a chronic lack of men, money and materiel. And on September 16, Putin ordered that the Russian army be expanded by 180,000 active-duty troops for a total of 1.5mn soldiers, making Russia's military the second largest in the world, behind China.

China is likewise investing heavily into its military and its navy is now larger than that of the US, as it adds the equivalent to the French navy to its fleet every four years, among other things. And now China is chasing the US submarine fleet, rapidly ramping up its submarine production.

Bankruptcy and recession

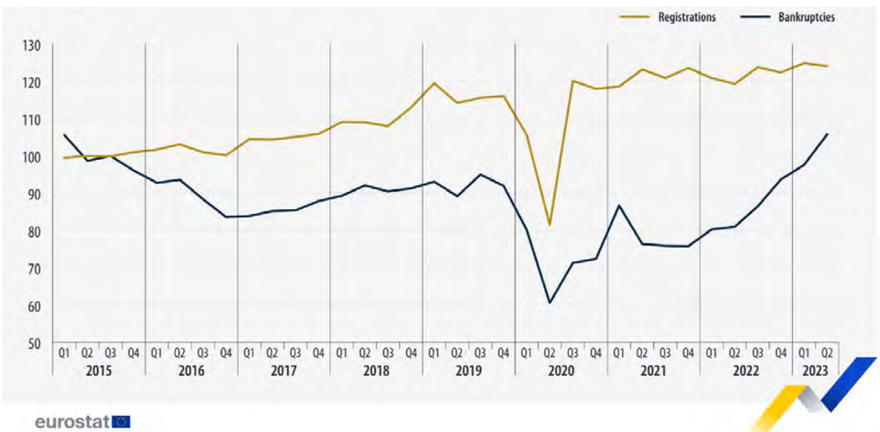
Europe is teetering on the verge of recession, while the Russian economy is booming – for now. That is sending more and more European companies into insolvency, as the economies adjust to a lower growth trajectory. Over the past three years the EU has seen a significant rise in bankruptcies, reaching record levels in 2023. What started in heavy industry becoming unprofitable has now spread to the lighter end of the industrial spectrum.

In 2023, EU bankruptcies surged for the sixth consecutive quarter, with an 8.4% increase in the second quarter compared to the previous quarter, reaching the highest level since data collection began in 2015, reports the European Commission. The number of bankruptcy declarations at the end of 2023 was above the pre-pandemic period levels recorded between 2016 and 2019, although the pace of bankruptcies started to slow towards the end of 2023.

Notably, industries such as accommodation and food services, transportation and storage have been hit hard this year, with increases of up to 82.5% compared to pre-pandemic levels in 2019 across the EU.

Some of these bankruptcies are a result of the slowdown or high energy prices. Others are due to the growing competition from emerging markets,

Registrations of businesses and declarations of bankruptcies in the EU Q1 2015 - Q2 2023, seasonally adjusted data (2015=100)



which are going up the value chain. Germany invented commercial solar panels and was home to a vibrant automotive sector. Both are now in trouble as they are overtaken by Chinese producers. Germany's solar panel business is now a wasteland after the government decided not to bail it out with subsidies, conceding defeat in the face of an unwinnable fight against higher Chinese quality and lower prices. As previously mentioned, China has become a manufacturing powerhouse and beats Germany not only on the technology of the panels themselves, but also with superior solar panel manufacturing technology to make them.

The double whammy of higher costs at home and increased competition abroad has put the export-orientated Germany SMEs in the front line. Many of them work in light manufacturing, whereas elsewhere in Europe SMEs are dominated by services. In 2021, the average number of bankruptcies in Germany was 1,000 per month. In 2024, this figure is approaching 2,000 per month.

The number of major bankruptcies in Germany also grew by 41% year to date. Household names that were set up over hundred years ago have gone bust in the first half of this year. Amongst the collapses were paper manufacturer ISHPaper, founded in 1828; shipyard Meyer Werft, founded in 1795; the butcher's chain Holzapfel Thüringer, founded in 1827; and the brewery Brauerei Bruch, founded in 1702, to name a few.

The story is the same in France, the UK and US. American bankruptcy filings surged over the past three years, reaching a 13-year peak in 2023. High inflation, high interest rates and the after-effects of the COVID-19 pandemic have contributed to this trend. The healthcare, consumer discretionary and industrial sectors were among the hardest hit. The number of corporate bankruptcies in France has surpassed the record set after the 2008 financial crisis. And the UK currently has the highest number of bankruptcies in 30 years after 25,158 registered companies became insolvent in 2023, *Bloomberg* reports.

All the main European economic sentiment indicators are falling, according to Oxford Economics. "The September decline in the ZEW Index provided another gloomy signal for the eurozone's near-term outlook. The drop was particularly large in Germany, where the assessment shows current conditions are now close to the lows of the pandemic," Oxford Economics said in a note in September.

The same goes for Emerging Europe, where the EBRD just downgraded its economic forecast for the entire region. In the latest Regional Economic Prospects report released on September 26, the EBRD projects growth of 2.8% for 2024, a slight reduction from its previous estimate of 3.0% in May 2024. The forecast for 2025 has also been revised downward by 0.1 of a percentage point to 3.5%. EBRD chief economist Beata Javorcik warned that "ongoing vigilance will be required as economies adapt to challenges related to renewed inflationary pressures, energy security, trade and financing conditions".

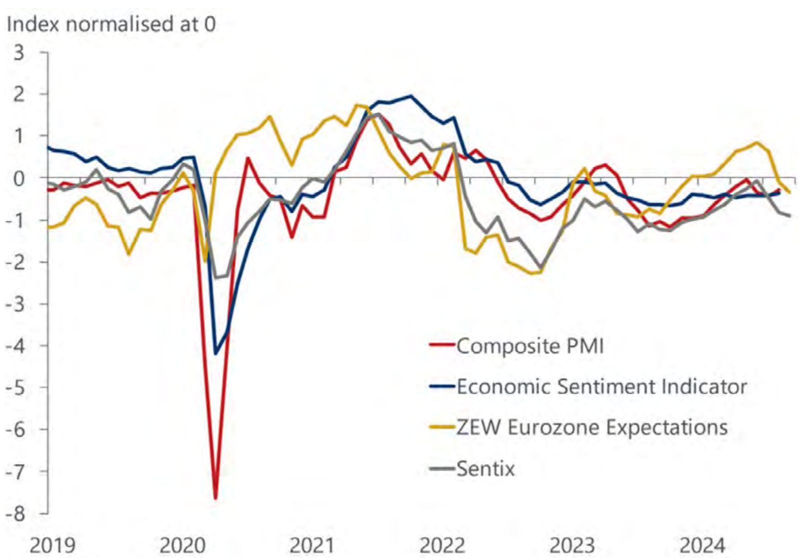
Even Russia is not getting off scot-free. Due to the exceptionally high key rate (19%), with which the Central Bank is trying to combat inflation, Russian companies are finding it increasingly difficult to service loans, according to a recent report by the Centre for Macroeconomic Analysis and Forecasting (CMAF). After unexpected strong growth over the last two years thanks to the war spending bump, Russia's economy is cooling as the military Keynesianism boost starts to wear off. The Central Bank of Russia (CBR) issued a pessimistic medium-term macroeconomic outlook at the start of August that predicts growth and consumption will slow dramatically starting in 2025.

On average, every fourth ruble of profit in the manufacturing industry goes to pay interest, analysts calculated. In 2023, the profit of Russian companies grew by 35%. But in the first quarter of 2024, compared to the same period last year, the figure fell by almost 4%.

But Russian companies are not going bust. In 2021, corporate bankruptcies in Russia increased modestly, up 3.9% from 2020, as part of a post-pandemic bounce back. In 2022 and 2023 there was a sharp decline in corporate bankruptcies, primarily due to government interventions such as a moratorium on insolvencies for key industries. By 2023 the number of company bankruptcies had dropped even further, by nearly 30% year on year, as the war boom got under way. Russia's economy still has a lot of leeway, despite the global slowdown, thanks to good management and lots of cash in reserve.

The current growth decline for the G7, on the other hand, is far worse – worse

Eurozone: Key surveys



GDP growth for leading economies of the world % y/y

	2020	2021	2022	2023	2024 Forecast
Germany	-4.6%	2.6%	1.8%	0.2%	0.6%
France	-7.9%	7.0%	2.6%	0.7%	0.9%
Italy	-9.0%	6.6%	3.7%	0.6%	0.8%
Spain	-10.8%	5.5%	5.5%	1.9%	1.5%
UK	-9.3%	7.6%	4.1%	0.1%	0.6%
Russia	-2.7%	4.7%	-2.1%	3.2%	2.6%
China	2.2%	8.4%	3.0%	5.3%	4.7%
Japan	-4.6%	1.7%	1.0%	0.9%	1.0%
Canada	-5.2%	5.0%	3.4%	1.5%	1.4%

Source: National governments

than in the drubbing it took during the pandemic and the financial crisis of 2008.

In 2023, the combined GDP of the seven leading countries was estimated at 1.5% compared to the previous year. And the EU only just managed to avoid recession in 2023, achieving an average growth rate of a mere 1%. The fastest growing economy in Europe in 2023 was the small Balkan country of Montenegro, which expanded by 4.5%, but almost all the big EU members were growing at less than 1%.

The EU governments and the economic press talk about a European "recovery" that assumes a return to the status quo and doesn't acknowledge the fundamental changes that have happened to Europe's economic makeup as a result of the polycrisis.

The economic pain is already having political consequences that make implementing reforms hard. Across Europe there is a swing to the right, such as AfD's (Alternative für Deutschland) recent victory in German's eastern state regional elections that is splitting German Chancellor Olaf Scholz's ruling coalition, and a new right-wing government in France, the most right-wing since the Republic was founded, to name only two recent examples.

While the rich world is getting poorer, the poor world is getting richer and starting to overtake its more advanced peers. Russia overtook Germany to become the fifth biggest economy in the world in PPP (purchase power parity) terms two years ago and surpassed Japan to become the fourth largest economy in the world in adjusted terms this year. China is now the largest economy in the world in PPP terms, followed by the US and then India and Russia. Germany has fallen down the rankings and is now number six, while the birthplace of the industrial revolution, the UK, has been pushed out of world's top ten manufacturing nations by Russia and Mexico for the first time in decades.

And with India's GDP growth projected at 8.2% in the current fiscal year 2024-2025, the country's economy could become the third largest in the world in nominal terms by 2030-2031, S&P Global said on September 19, provided that reforms critical to improving business operations and logistics, stimulating private sector investment and reducing dependence on public capital continue. Both China and India are expected to become number one and two in nominal GDP terms sometime in 2070.

Other up and comers from the EMs include Indonesia and Mexico, which have been shooting up the rankings in recent years. Bangladesh is also an unsung success story (population 171mn) after per capita GDP in the country overtook that of India in the last few years, until the former was plunged into chaos after its Prime Minister Sheikh Hasina was ousted in August by violent protests.

At the geopolitical level there are also consequences to this game of economic musical chairs. The attempts to sanction Russia's economy into oblivion have backfired and catalysed China and Russia into beefing up their non-aligned multinational alternative centres of power, such as the BRICS+ and the G20.

Worried by the US decision to weaponise the dollar and freeze international reserves, the countries of the Global South are de-dollarising and flocking to these organisations, simply as a counterweight to an increasingly unpredictable America.

As the leading emerging markets climb up the GDP rankings, the appeal of the Moscow and Beijing-run clubs increases, as not only do they show that sanctions don't work if enough of the rest of the world ignore them, but that the Global South now represents the richer and faster growing half of the world. Collectively the BRICS

Top 15 countries GDP in PPP terms

Rank	Country	2023 GDP (PPP) ($bns)
1	China	34,643.71
2	United States	27,360.94
3	India	14,537.38
4	Russia	6,452.31
5	Japan	6,251.56
6	Germany	5,857.86
7	Brazil	4,454.93
8	Indonesia	4,333.08
9	France	4,169.07
10	United Kingdom	4,026.24
11	Turkey	3,767.23
12	Italy	3,452.51
13	Mexico	3,288.67
14	South Korea	2,794.20
15	Spain	2,553.11

Source: World Bank

alone account for 35% of global GDP in nominal, not adjusted, terms, whereas the G7 accounts for 30%, as Putin keeps pointing out. And the BRICS have ten times the population of the G7. Russia remains by far the largest consumer market in Europe with 145mn people, followed by Germany with 83mn.

The BRICS+ club has already been expanded to include 10 members at last year's gathering and 17 more countries have applied to join at this year's summit hosted by Russia in Kazan in October, with another 22 countries in the wings. Azerbaijan, Indonesia, Malaysia and Turkey are amongst those that are expected to join this year. One of the first things the expanded BRICS+ intends to do is build a BRICS currency to replace the dollar in international trade.

Colonialism and comparative advantage

The French are good at making champagne and the most profitable British export is the Rolls Royce car. A basic tenant of economics is "comparative advantage": instead of Frenchmen making champagne and cars, they should put all their effort into just making champagne and leave the Brits to make the Rolls Royces, who can import all the champagne they need. The net result is both the French and the British net-net have more champagne and cars. Sanctions have destroyed this equation that is at the heart of the globalisation.

Running even deeper than comparative advantage is the net transfer of wealth from the Global South to the rich markets of the North. As *bne IntelliNews* reported, for the last 500 years or so there has been a net transfer of wealth from the Global South to the developed world, pioneered in the empire-era. Economists say there have been three globalisation periods: 1870-1914, 1944-1971 and the most recent, which is still ongoing, started in 1989 but is winding down now.

The West exports some 90% of its manufacturing capacity to the Global South but the Global South only receives 21% of the revenues generated, according to a study published in *Nature Communications* in July.

In effect, the Global South has exported its human capital to the West and, thanks to the huge discrepancy between wages, it is very badly paid for it, according to the study. This colonialist transfer is the basis of the West's relative wealth compared to the Global South and the raison d'etre for empires, which have been replaced by multinationals.

This set-up is starting to finally break down, first due to the onshoring due to the pandemic and then to the "friendshoring" due to the geopolitical tensions in an increasingly fractured world. The same study found that not only are the manufacturing exports no longer just targeting low-cost, low-skill manufacturing, but increasingly the emerging markets are providing high-skilled production, and wages are rising in these countries.

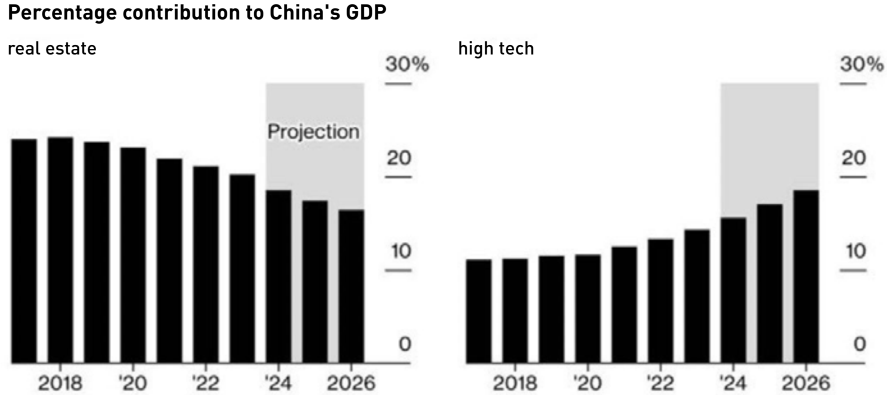
This story has already played out in Poland, where wages have risen to match the EU average as firms have gone up the value chain, making Poland one of the most robust economies in Europe. And it also played out in Russia, where wages have risen relentlessly from next to nothing in 1991, after Putin spent a decade boosting public sector wages by 10% a year in the noughties to close the burgeoning gap between the public sector and private to avoid social unrest. The average salary in Russia today is just under RUB90,000 ($964) a month, which is $2,185 in PPP adjusted terms, which is almost exactly the same as the EU average salary of €2,006 ($2,240). However, there are still significant regional differences. In particular, salaries in Moscow are much higher and can reach RUB360,000 ($4,700) a month and more for things like IT experts, bankers and other professional jobs, according to the Average Salary Survey. Overall, Russian's incomes are now on a par or higher than that of the EU and salaries in the capital are on a par with those in cities like London, Paris and Berlin.

China is also well advanced in this process. Its rapid catch-up in the last few decades has been driven by being the "factory of the world," but the relentless rise of wages means about a third of the population now earn Western standard middle-class wages. China has gone from "made in China" to "created in China."

Russia used to import its manufactured goods from China like everyone else, but in the boom years of the noughties, Chinese wages overtook Russian wages, spurring an expansion in light manufacturing investment in Russia as it became cheaper for Russians to make the goods themselves. Under China's new economic development plan the emphasis has switched from an export-orientated model to an innovation-orientated model. The share of Chinese GDP from high tech is expected to exceed that of real estate in the next two years, when just six years ago real estate was still twice that of high tech, *Bloomberg* reports.

All of the countries of the Global South are being lifted by the same tide, but increasingly they resent the colonialist model that has robbed them of their human capital wealth, and they are

Percentage contribution to China's GDP



Source: Bloomberg Economics

starting to push back, which is also fuelling the gravitation to things like the BRICS+ and G20 groups.

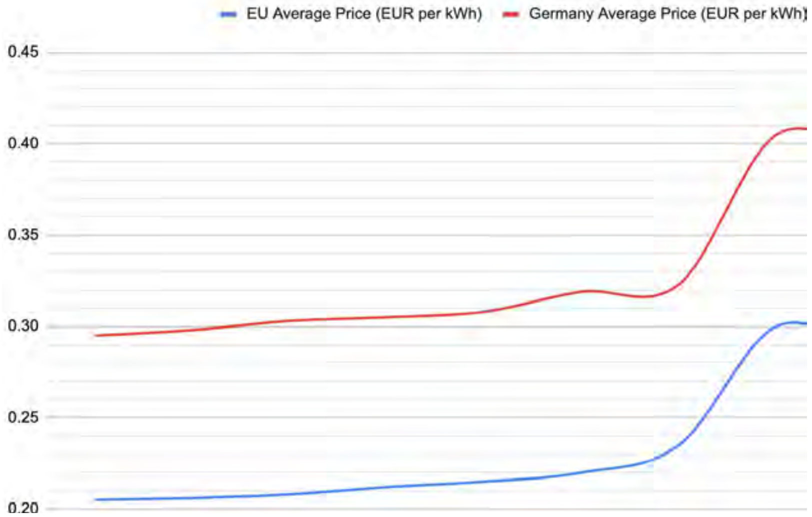
A former colony, Niger has long been a French client in Africa, but earlier this year a new government kicked France out of the country, despite Paris' loud prostrations. Niger also happens to be a major source of uranium and 80% of France's power is nuclear. But France was reported only playing a fraction of market prices of supplies of uranium from Niger.

The countries of the Global South are becoming increasingly resentful of this colonialist model, particularly in Africa, that has been sanitised in the West with the "globalisation" label. The wealth transfer remains an exploitation of labour and a theme that the Kremlin plays on constantly to a warm reception outside the Western world. As *bne IntelliNews* reported, French President Emmanuel Macron got roasted by Felix Tshisekedi, the president of the Democratic Republic of Congo, live on TV last year during an official visit as the French president tried to shore up relations with France's former colonies.

"This must change, the way Europe and France treat us. You must begin to respect us and see Africa in a different way," Tshisekedi told Macron to his face with the cameras rolling. "You have to stop treating us and talking to us in a paternalistic tone. As if you were already absolutely right and we were not."

The same resentment is behind Russian Foreign Minister Sergei Lavrov's "new rules of the game" speech in February 2020, which was the starting point of an escalation in tensions that ended in the invasion of Ukraine two years later. Lavrov said that Russia would no longer tolerate the West's dual approach of sanctioning Russia with one hand but doing business with the other. He threatened to break off diplomatic relations if this didn't change. Russia and much of the Global South object to the right the West gives itself to lecture and sanction them on things like LGBT rights, but at the same time ignore all criticism on issues like US' material support of Israel's bombing of Gaza.

European vs German power prices 2019-2023 (EUR/kWh)



Source: European Commission

This dichotomy is increasingly seen by many in the Global South as the hypocrisy of a two-speed world, divided into the haves and have-nots, and was made doubly poignant when the US was downgraded to "flawed democracy" by the respected EIU in 2016.

"The war in Ukraine is a European problem, caused by Europeans. Let Europe fix it! I don't think that India should become involved at all," Bhaswati Mukherjee, former Indian ambassador to the EU and UNESCO, told *bne IntelliNews* in a recent interview, following suggestions that Indian Prime Minister Narendra Modi is the best placed international statesman to mediate a peace between Ukraine and Russia.

The Kremlin became equally fed up with being talked down to but after three decades thanks to the stability Putin brought it is more or less a normal country in terms of income, on a par with the rest of Europe in real terms and increasingly on nominal terms too.

As wages rise relentlessly in the Global South, the wealth transfer from south to north will slow as the income gap closes, pushing up the cost of imported goods, while the profits from the export of manufacturing slowly fall. There is little the West can do to prevent this change other than keep its technological and productivity lead.

But it is going to be a long, slow and difficult process. The Global South is already trying to coordinate this change with a raft of new non-aligned organisations such as the BRICS+, the G20, the Shanghai Cooperation Organization (SCO), MERCOSUR, ASEAN, the African Union and many others, but it is still early days and regional rivalries, such as those between China and India, remains problems.

Food price inflation

Food price inflation is one the permeant changes that will only make the cost-of-living crisis worse thanks to a combination of Climate Crisis-related falling agricul-tural yields and disruptions to trade with Russia and Ukraine – the two largest tradable food producers in the world.

Russia is commonly seen as a provider of oil and gas, but thanks to a decade's worth of heavy investment it has also become a global agro-power. In 2023, the volume of agricultural supplies to foreign markets amounted to $43.5bn. In total, Russia exported more than 100mn tonnes of food. But, like oil, those exports are now going to new markets.

The cost of Britain's iconic fish & chips has doubled as it remains heavily dependent on the import of Russian cod, while German fishmongers are preparing for thousands of layoffs.

"The German market depends on fish from Russia. We cannot do without saury and cod," explained Steffen Meyer, director of the Federal Association of the German Fish Industry and Wholesale Trade. Russia itself set a record for seafood exports in 2023 and is projected to earn $5.6bn in 2024, after exports were redirected to Asia.

The FAO Food Price Index (FFPI) has been declining since its spiked in March 2022, caused by the start of the war in Ukraine. However, while global prices have eased, food price inflation remains a serious problem, particularly in low- and middle-income countries. For example, food price inflation was still above 30% in several nations, such as Ethiopia, Ghana and Sudan, by late 2023. High-income countries have seen a slower rise in food costs, with inflation dropping to around 3.8% by late 2023, according to IFPRI, but the relentless rise is adding to the cost-of-living crisis in Europe.

As *bne IntelliNews* reported, over a billion people's food supplies around the world are threatened by the accelerating climate crisis and up to 4bn people are now suffering from poor nutrition in some of the poorest countries in the world.

India suffered from a rice crisis last year, adding to the overall price increases as extreme temperatures saw yields plunge there too, causing the government to ban exports to prevent a price spike. The tomato crop in India failed completely. Food insecurity is not only caused by the lack of food, but also spikes which increase food prices to beyond the level the poorest members of society can afford to pay. Grain yields in both Ukraine and Russia have been falling in the last two years.

Russia brought in a record harvest of 153mn tonnes, smashing even Soviet-era records, in 2023, but this year the harvest is expected to fall back to 132mn tonnes as yields retreat due to the extreme temperatures following the hottest summer on record in 2024. The way agricultural markets work, if Russia's export grain price firms then grain prices around the world rise as well.

Climate crisis-driven global food security has already deteriorated between 2019 and 2022 and is even already affecting the US and Europe, where agricultural yields are down by more than 30%, according to scientists. Storms in Europe destroyed €9.1bn worth of property in 2023, while the US saw 28 separate weather disasters costing at least $1bn a piece. When the results come in from this year, including the destruction caused by Storm Boris, they are likely to be worse. Scientists predict that the frequency and power of extreme weather events during what will now be an annual disaster season will only get worse from here.

Estimates vary, but recent studies published in Nature Food, NASA and Springer Link, estimated strained population will demand 35% – 56% more food from crops that will yield dramatically less and be less dense in key nutrients. After some short-term gains for Europe (as a warmer Europe means more winter crops), food security is only going to become a bigger issue as time goes on and Russia's massive surplus of grain production more important.

The record-breaking heatwaves and prolonged droughts in Europe in the last two years have hit Southern and Eastern Europe more than the North, reducing yields in crops like wheat, maize and barley. The European Commission reported that the 2022 drought reduced cereal yields by 10%, with maize production falling by nearly 16%, according to the World Bank.

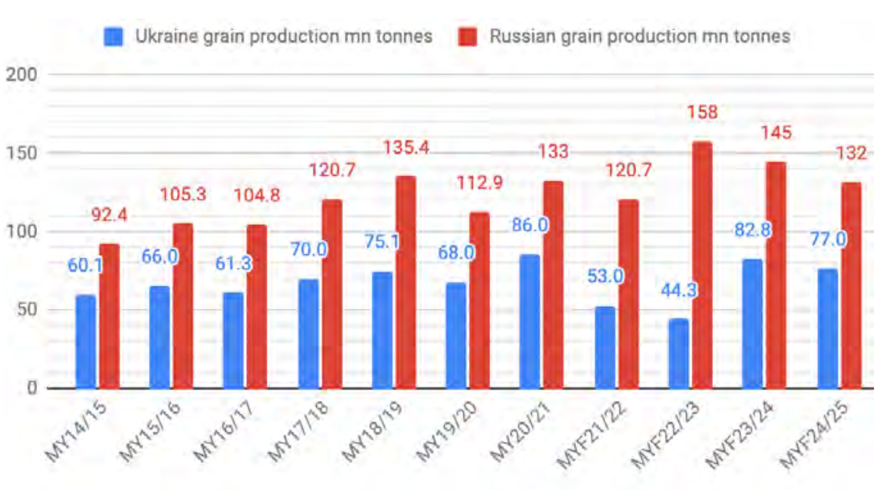
Some regions, particularly in Northern Europe, may initially benefit from warmer temperatures, allowing for extended growing seasons. However, the long-term consequences of more frequent extreme weather events outweigh these benefits, says IFPRI. Wheat yields have been particularly vulnerable to heatwaves and droughts. France, one of the EU's largest wheat producers, has seen reduced yields in recent years. The drought of 2022 was particularly damaging, with wheat yields falling by 5-10% across Europe.

FAO Food Price Index

Year	FAO Food Price Index (2014-2016 = 100)
2015	93.0
2016	91.9
2017	98.0
2018	95.9
2019	95.1
2020	98.1
2021	125.7
2022	160.3
2023	124.7
2024 (YTD)	120.7

Source: UN Food and Agriculture Organization

Ukrainian and Russian grain production, mn tonnes



Source: bne IntelliNews

Cost-of-living crisis

The rising food prices are already affecting consumer behaviour. In the US, the Dallas Federal Reserve released a study that found the sale of sausages has soared; economists say the reason is because the price of meat has risen so much that punters are trading down to sausages as the cheapest form of meat on the market.

At the same time, the US Restaurant Performance Index (RPI) fell -1.3% in July to 97.7 points, the lowest level since the 2020 lockdowns, as punters stay in more. Since 2021, this metric has fallen by ~8.0%, marking the largest drop since it was launched in 2002. Since 2020, food prices away from home have gained 27.0%, and fast-food prices have jumped by 31.0%, far in excess of the rise in basic inflation.

In general inflation in the G7 is running much higher than the developing world, although thanks to overheating Russia's inflation is a persistently higher, at around 9%, but still less than the rising in nominal wages of 12%, resulting it soaring real disposable incomes up to a record 9.6% in July. The upshot is that while prices are rising fast, income is rising faster and instead of a cost-of-living crisis, Russia is enjoying a consumer boom.

The Eurozone retail sales continued to flatline in the second quarter with a negatable 0.1% rise in retail trade for July, adding to the cost-of-living pressures, according to ING. Draghi says that real disposable incomes in the US have grown twice as much as in the EU since 2000.

Inflation has outpaced wage growth, resulting in a decrease in real wages – the purchasing power of incomes adjusted for inflation. For example, in the United States, while nominal wages increased by about 5% in 2022, inflation was higher at 6.5%, leading to a decline in real wages.

One of the areas where the cost-of-living crisis is being felt most acutely is in the rapid rise in housing prices. Frustrated US millennials, who need to earn at least $110,000 a year to be able to buy a house, complain that they cannot afford to buy anymore. House prices climbed by 6.6% over the last year, with a 5-year growth of 7.1%, driven by high demand despite rising mortgage rates.

In Europe real wages actually fell by 2.4% in 2022, the steepest decline in decades, that came on top of soaring food prices. Yet house prices continue to climb strongly, outpacing the increases in average incomes over the last five years, despite softening somewhat in the last year due to the economic slowdown. Germany has been one the most affected, where house prices jumped by 56% between 2010 and 2022.

Italy is the exception, where house price inflation has fallen over the last two decades, but young would-be homeowners are facing a different set of cost-of-living problems that have depressed fertility rates to become the lowest in Europe: the Italian replacement rate is currently running at only 1.2 as young couples simply can't afford to have a second baby. Draghi pointed out in his report that Europe is suffering from a demographic crisis, as no country has a replacement rate

Inflation rates in leading economies

Country	Inflation Rate (2023-2024)
United States	3.2% (2024 projection)
Canada	3.3% (2024)
United Kingdom	6.8% (2023)
Germany	6.1% (2023)
France	4.9% (2023)
Italy	5.6% (2023)
Japan	3.1% (2023)
Russia	9.1% (Aug 2024)
China	0.6% (Aug 2024)

Source: Trading Economics

Major economies housing prices, change in income 2019-2023 change

	Year-on-Year Change in House Prices (2023)	5-Year Change in House Prices (Inflation-Adjusted)	5-Year Change in Average Income
Germany	-2.0% (Decline due to economic slowdown)	+16.88%	+9.1%
France	+3.1% (Urban demand)	+16.22%	+8.2%
Italy	-8.0% (Weaker demand)	-5.16%	+2.5%
Poland	+13.0% (High demand)	+11.86%	+10.2%
Hungary	+9.5% (Strong rise in Budapest)	+13.41%	+8.9%
Czechia	+4.8% (Stable increase)	+13.13%	+7.5%
United Kingdom	+4.5% (Limited supply)	+9.48%	+4.6%
China	-5.3% (Decline amid real estate slowdown)	-3.7%	+7.8%
Russia	+9.7% (Housing boom in urban areas)	+23.1%	+12.5%
United States	+6.6% (Steady appreciation)	+7.1%	+9.0%

Source: UN Food and Agriculture Organization of over 2.1 births needed to keep the population stable.

Unsurprisingly the demographics in Ukraine are a catastrophe: Ukraine has the highest mortality rate and lowest fertility rate in the world – three deaths for every birth – according to the CIA factbook.

China is also suffering from a low fertility rate thanks to its previous "one child" policy, but Russia has seen its fertility rate increase in recent years from 1.4 to the current 1.83 thanks to Putin's babies, the Kremlin's highly successful natal support reforms that Putin introduced in his first term in office. As detailed in *bne IntelliNews*' latest despair index (the sum of poverty, unemployment and inflation), Russia currently has its lowest level of despair since 1991 despite the strains of war, and is well ahead of most of Europe.

Permanent increase in energy costs

Rising energy prices are the obverse side of the coin to the rising food prices that have been permanently changed but the polycrisis. The cost of power in Europe spiked 20-fold in in 2022 but has since fallen back. But it has not fallen back to where it was in 2021.

High energy costs are a serious problem for Europe, but not for the self-sufficient US and Russia. The end of cheap Russian gas supplies, particularly to Germany, has caused a permanent change to the structure of Europe's energy market and power prices remain double what they were pre-war.

"The price differential vis-à-vis the US is primarily driven by Europe's lack of natural resources, as well as by Europe's limited collective bargaining power despite being the world's largest buyer of natural gas," says Draghi. "However, the gap is also caused by fundamental issues with the EU's energy market. Infrastructure investment is slow and suboptimal, both for renewables and grids. Market rules prevent industries and households from capturing the full benefits of clean energy in their bills. Financial and behavioural aspects of derivative markets have driven higher price volatility. Higher energy taxation than other parts of the world adds a tax wedge to prices."

"The price differential vis-à-vis the US is primarily driven by Europe's lack of natural resources, as well as by Europe's limited collective bargaining power despite being the world's largest buyer of natural gas"

To highlight the increased energy uncertainty, Europe may see a large 66-78mn cubic metres a day shortfall – equivalent to a third of the UK's consumption – this winter after Norway announced unscheduled pipeline maintenance work on September 26, coupled with Armed Forces of Ukraine (AFU) advances in Russia's Kursk region near the Sudzha gas pumping station and disruptions to global LNG supplies due to hurricane Helene in Mexico.

In 2023, Germany consistently had the highest household electricity prices in the EU, reaching €0.40/kWh. Nuclear-powered France, on the other hand, maintained lower prices but saw a significant increase due to the energy crisis. Spain saw a large rise in 2022 but experienced a decrease in 2023, aided by government measures. The UK also saw steep rises during this period.

While prices moderated in 2023, high volatility persisted, particularly in the day-ahead and intraday markets. Negative prices (where electricity prices fall below zero) have occurred frequently, reflecting supply-demand imbalances, especially during periods of excess renewable energy production.

In countries where natural gas is a primary source for electricity generation, the wholesale electricity prices used by industry also surged, with some industries seeing wholesale electricity prices jump by 300% to 500% by the end of 2022 in certain countries.

To mitigate the effect of rising energy costs on industries, many governments introduced subsidies, price caps and financial support, but that has not shielded industry entirely from the price hikes.

Wholesale electricity prices in 2023 began to stabilise but remained elevated compared to pre-2020 levels, particularly in Europe and Asia. Businesses in the UK currently pay the most for wholesale power, whereas Germany is somewhere in the middle of the range. In the US and some other regions, prices for industrial power remained lower due to a more diversified energy mix and access to domestic energy resources like shale gas. Industrial power costs in Europe are anticipated to remain volatile in 2024.

Germany's industrial sector is highly energy-intensive, with demand patterns that can shift rapidly, so as industry recovered in 2023 it putting further

Major economies fertility rates, births per women

Country	Fertility Rate (2024)
France	1.9
Germany	1.5
Italy	1.24
Spain	1.16
EU Average	1.46
UK	1.6
United States	1.84
Russia	1.83
China	1.5

Source: World Population Review, Our World in Data, CIA strain on the supply side of the market and increased price volatility that the US and Russia don't suffer from.

The EU is the largest global gas and LNG importer. It has little gas of its own and what it does have is in decline now The Netherlands' large Groningen natural gas field and the UK's North Sea fields are exhausted. The differences in what Europe pays for energy and what the US and emerging markets pay is a millstone around European companies' necks. Russia has always enjoyed cheap energy, but now it is selling it to the friendly countries at a steep discount, handing them an extra competitive advantage on top of their already low labour costs. The US also enjoys much cheaper energy.

Russia, with its copious supplies of gas and nuclear power plants (NPPs), has long enjoyed an energy dividend in manufacturing. And since China became the global green energy champion producing the majority of the world's renewable energy, it is seeing its energy costs tumble.

"EU companies face electricity prices that are two to three times those in America. Natural gas prices are four to five times higher. Over time, decarbonisation will help shift power generation towards secure, low-cost clean-energy sources," says Draghi. "But fossil fuels will still set the energy price for most of the time for at least the remainder of this decade. Unless Europe better transfers the benefits of clean energy to end-users, energy prices will continue to dampen growth."

Germany has been particularly hard hit, as since it phased out its six NPPs in 2023 – the largest and most efficient in Europe – it has gone from a net exporter of electricity to a net importer of around 11.7 TWh a year. The German shortage is indeed a problem for Germany, but it is an even bigger one for Italy, Austria and Luxembourg that have all become dependent on German power exports to cover their own deficits.

SMEs have been particularly hard hit in Germany, France and other EU states, making formally profitable businesses loss-making.

Mittelstand firms are highly export-oriented, which exposes them to global market competition. Economic disruptions, like supply chain bottlenecks due to the war in Ukraine and trade disputes with China, coupled with rising energy prices and a labour shortage thanks to the poor demographics, have all combined to hurt their operations and profitability. The Mittelstand is in the backbone of Germany's economy, making up 52% of GDP in 2023, and now company after company, particularly in light manufacturing and machine building, is going bust.

"Electricity prices [in Germany] have stabilised somewhat, partly because gas prices have become more stable and because of a decline in industrial activity. The cost of CO_2 emissions permits has also dropped significantly. However, electricity prices are still two to three times higher than they were before 2021," says Holger Zschaepitz, the markets editor at Die Welt. "That's hurting everyone."

That is not going to change, as Russia is in the process of switching its energy export infrastructure – 70% of which used to go to Europe – from west to east. Moreover, this permanent change to the global energy markets, coupled with sanctions means the Global South now enjoys a discount while Europe is stuck paying a premium.

Russian gas to Europe is gone, but the oil sanctions have failed to stop Russia making money from exports. They are not sanctions, but a huge market distortion. Oil that used to travel a week from Primorsk in the Gulf of Finland to the ports in Rotterdam now takes a four-month journey to refineries in India and China before returning to the European markets as petrol. It's the same Russian oil, but the trip whitewashes its identity in the name of "sanctions" designed to reduce the Kremlin's income. Russia is still earning hundreds of billions of dollars from oil exports and is running a healthy current account surplus and

Average cost of electricity per kilowatt-hour (kWh) for the period between 1995 and 2020

Country	1995-2020 Average (€/kWh)	2020 (€/kWh)	2021 (€/kWh)	2022 (€/kWh)	2023 (€/kWh)
Germany	€0.23	€0.30	€0.32	€0.34	€0.40
France	€0.15	€0.18	€0.19	€0.21	€0.25
Italy	€0.19	€0.23	€0.23	€0.32	€0.35
Spain	€0.18	€0.23	€0.24	€0.31	€0.24
EU Average	€0.19	€0.21	€0.23	€0.28	€0.29
UK	€0.16	€0.21	€0.22	€0.28	€0.34
US	€0.11	€0.13	€0.14	€0.15	€0.17
Russia	€0.05	€0.06	€0.06	€0.07	€0.08
China	€0.07	€0.08	€0.09	€0.10	€0.11

Source: European Commission

a small budget deficit that is paying for its war.

The upshot is that the West is now paying a premium for its oil, whereas the friendly countries in emerging markets are now enjoying a discount on the most basic input: energy. According to the last KSE study, the discount Russia offers its friends in Asia has tightened recently but it's still $11 on a barrel of oil, or about 10% less, which a major competitive advantage. And as Russia continues to build its new distribution system these changes will be hard baked in and will not only apply to oil, but a whole smorgasbord of essential commodities.

Deficit Europe

Food and energy prices are up, and now key raw materials are going missing. Putin demanded that the government draw up a roadmap to restrict strategic raw materials to external markets on September 14, including uranium, nickel and titanium, just as the US was mulling granting Ukraine permission to use its long-range missiles to strike targets deep inside Russia.

"This marks the beginning of Russia's transition from exploiting energy dependence on the West to manipulating the market for critical raw materials. As the EU is set to gradually abandon Russian energy resources, Putin is trying to spot other vulnerabilities in the strategic dependence on the West. This could be inspired by the Chinese approach, which restricted the export of processed graphite in 2023. Controlling 90% of the supply, China's decision came at a high cost for global EVs production," says political analysts and *bne IntelliNews* columnist Denis Cenusa.

Europe has a raw materials deficit. After 500 years of wealth flooding into the Continent from colonialism, Europe is extremely densely populated – too densely. Western Europe ranks second in terms of population density among continents after Asia, with 180 people per square kilometre, but less in the south and east of the region.

The Continent doesn't have anywhere near enough natural resources to sustain itself and so has to import a large part of what is needs. The EU relies heavily on imports of agricultural and energy commodities to meet its demand, as well as metals and chemicals from Russia and food stuffs like cocoa and soyabeans from the rest of the world.

For other products like timber and sugar, domestic production covers a larger share of demand, but not all. For example, the EU needs to import 86% of its soyabean needs, essential animal feed, while its own timber resources have long been maxed out and any growth in demand has to be sourced from elsewhere – previously from Russia's leading wood products giant Segezha.

The EU produces around 160mn tonnes of steel annually but imports significant quantities from countries like China and Russia, which account for around 18-20% of its total steel consumption.

The situation with more specialist metals is more dramatic. Production of titanium, essential for aircraft production, is minimal, and 90% of the EU's titanium consumption is imported from Russia. Power-hungry aluminium is a little better, and the EU produces around 7mn tonnes per year (tpy), but another 45-50% of its needs is met by imports, mainly from countries like Norway, China and Russia, according to the European Commission.

> "This marks the beginning of Russia's transition from exploiting energy dependence on the West to manipulating the market for critical raw materials"

Russian aluminium is another "unsanctionable" export item: "The EU is toying with the idea of slapping sanctions on one of Russia's most important exports to Europe: aluminium. If it happens, the end of aluminium deliveries to Europe could cause prices to spike and drive smaller companies out of business, as there are few alternatives to Russia's aluminium," says Chris Weafer, the founder and CEO of Macro Advisory and former head of research at multiple Moscow-based investment banks.

The US doesn't suffer from these problems, as it is almost entirely self-sufficient in everything, with a few notable exceptions like uranium.

This list of commodity imports was collectively worth €212bn in 2023, which was about 10% of the total EU import business from external markets of €2.75 trillion, according to European Commission.

The ineffectiveness of sanctions and the West's continued dependency on some key Russian inputs can be illustrated by the trade in LNG, fertilisers and uranium.

LNG: The European Parliament called for an embargo on Russian LNG and sanctions against Gazprom on September 19 by adding Russia's Arc-7 ice-class ships that export Russian LNG and the rest of the world. However, as *bne IntelliNews* reported, Europe remains hooked on Russian gas, still buying 25 bcm of gas (18 bcm of LNG, 8 bcm of piped gas) that still makes up some 20% of the EU's total gas imports, down from 45% pre-war. Russia is successfully replacing the gas that used to be piped via Nord Stream with LNG shipments.

LNG imports to the EU took off in 2022, according to Gas Infrastructure Europe (GIE), up 1.7-fold compared to the 2021 level to 127.2 bcm from all sources (mostly US and Qatar) – almost as much as Europe imported from Russia pre-war.

European commodities production and import data 2023

Commodity	EU Production Volume	EU Import Volume	Import Value (€)	Import Share (%)
Crude Oil	~20mn tonnes	~425mn tonnes	€22.9bn (Q2 2023)	~95%
Natural Gas (inc LNG)	~50bn m³	~330bn cubic metres	€150bn	~85%
Coal	~60mn tonnes	~140mn tonnes	~€16bn	~70%
Soybeans	~2.5mn tonnes	~15mn tonnes	~€3bn	~86%
Palm Oil	Minimal	~7mn tonnes	~€3bn	~95%
Coffee	Minimal	~3.5mn tonnes	~€4bn	~100%
Cocoa	Minimal	~2.5mn tonnes	~€6.5bn	~100%
Sugar	~20mn tonnes	~3mn tonnes	~€2bn	~13%
Timber	Significant domestic	~5mn cubic metres	~€8bn	~20%
Steel	~160mn tonnes	~36mn tonnes	~€40bn	~18-20%
Titanium	Minimal (mostly imported)	~13,000 tonnes	~€1.8bn	~90%
Aluminium	~7mn tonnes	~5.5mn tonnes	~€10bn	~45-50%
Electronic Components	Limited	Significant imports	~€50bn	~85%
Fertilisers	~17.3mn tonnes	~10mn tonnes	~€12bn	~30-35%

Source: Eurostat, European Commission (EC), Centraal Bureau voor de Statistiek

Fertilisers: Russian fertiliser sales to the EU are also booming as Europe has few alternative sources. From January to May 2024, Russia exported 1.9mn tonnes of fertilisers to the EU, driven largely by high natural gas prices that have forced European chemical factories to reduce their own fertiliser production.

Fertilisers remains a business dominated by Russia and Belarus. Previously Europe imported a third of its fertiliser needs, but as gas is a major input and gas prices have soared, Europe's own fertiliser makers were amongst the first heavy industry facilities to shut down during the energy crisis of 2022. In 2022, the value of fertiliser imports reached approximately €12bn, with imports making up about 30-35% of the total fertiliser consumption in the EU. The list goes on.

The demand for Russian nitrogen fertilisers rose by 39%, amounting to 1.1mn tonnes during the first five months of 2024. Poland emerged as the largest importer, accounting for 25% of these imports, followed by France (12%), Germany (11%) and Italy (10%). In addition to nitrogen fertilisers, there was a significant increase in the import of potash and complex fertilisers. Potash fertiliser imports from Russia to the EU quadrupled to 182,500 tonnes, while complex fertilisers saw a twofold increase, reaching 619,600 tonnes. The EU has accounted for approximately 20% of global fertiliser imports over the past five years.

Historically, Russia has supplied about 13% of the EU's fertiliser imports between 2018 and 2021. Although this share dipped to 8-9% in 2022-2023, recently they have started to grow strongly as the EU's own production falls away. The EU initially included Russian fertilisers in its fifth sanctions package in April 2022, but quickly dropped the idea as unworkable. Projections suggest that Russian fertiliser exports could reach 44mn tonnes by the end of 2024, marking a 10% increase from 2023.

Uranium: Likewise, the US recently "banned" the import of Russian uranium; however, as the US doesn't produce any enriched uranium of its own to speak of, a system of waivers was introduced in parallel with the sanctions that allow US firms to continue to import Russian uranium until 2028. The US is at least five years away from becoming self-sufficient in the nuclear fuel.

Globally, Kazakhstan leads in the mining of uranium, but enrichment is currently dominated by a few key players. Russia holds about 40% of the global enrichment market, primarily due to its state-owned company, Rosatom. Other major players include Urenco in Europe and Orano in France, which account for about 12% of global enrichment capacity. The US currently produces only a small fraction of its needs domestically, relying on imports for around 30% of its enriched uranium, but recent efforts aim to expand domestic production.

No decision had been made at the time of writing, but even if Putin doesn't use uranium as a tit-for-tat political weapon, the threat highlights Russia's monopolistic power in the international commodities markets.

Tech race

Draghi's report puts technology prowess at the heart of his proposed solution to Europe flaccid growth. And it needs to be. The cost of production in Europe is twice as high as in the US and over three times more than in China, but the EU is badly trailing behind both the US and China on innovation, and China is rapidly catching up with the US.

"The report proposes a fundamental reform of the innovation lifecycle in Europe: from making it easier for researchers to commercialise ideas, to

Top ten countries patent filings 2019-2023

Rank	Country	Number of Patents Filed (2019–2023)
1	China	6,900,000+
2	United States	2,700,000+
3	Japan	1,900,000+
4	South Korea	1,400,000+
5	Germany	700,000+
6	European Patent Office	600,000+
7	India	500,000+
8	Russia	400,000+
9	France	300,000+
10	United Kingdom	250,000+

Source: World Intellectual Property Organization (WIPO) and other patent offices

joint public investment in breakthrough technologies, to removing barriers to scaling up for innovative companies, to investing in computing and connectivity infrastructure to lower the cost of developing AI," Draghi said. "A weak tech sector will not only rob it of the growth opportunities of the coming AI revolution. It will also hinder innovation in a wide range of adjacent sectors – such as pharmaceuticals, cars and defence – where integrating AI into operations will be critical for the EU to remain competitive."

Draghi focused on the competition between the US and Europe in his report, but it is the emerging markets that are the real competition. And Draghi is right: the only place Europe can compete, given its fixed material and power costs, is on productivity – labour is by far the biggest contributor to unit costs. Staying ahead in the technology race is the key to keeping Europe competitive.

Over the past three years, the number of tech IPOs in the US, China and Europe has been very varied.

China has dominated IPO activity globally, especially with its STAR Market and other tech-heavy exchanges. In 2023, there were 42 IPOs concentrated in tech hardware and services. The market saw valuations increase dramatically due to the sheer scale of listings, and in 2023 alone, China raised $45.3bn through IPOs, contributing to its robust tech sector growth.

The US tech ecosystem is much more mature than China's with a lot more companies coming to market. There was a boom in tech IPOs in 2021, with a record-breaking 126 tech IPOs. However, market conditions in 2022 saw a dramatic slowdown, with only 6 tech IPOs and a slow recovery in 2023 with major listings like Arm and others boosting confidence. Total funds raised through IPOs in the US in 2023 were approximately $17.57bn.

Europe is the laggard. The European tech IPO market is much smaller and any really successful venture usually chooses to list in the larger and more liquid New York market. In the peak year of 2021 there was an average of about 5 IPOs per month and companies like UiPath raised billions of dollars. The total market capitalisation for major European tech companies that went public in recent years is estimated at around €7.5bn.

But the pipeline in the US for more valuable tech IPOs is healthier than in China. As of 2024, the number of tech unicorns (privately owned companies valued at more than $1bn) in the US is the highest globally, with 720. China is in second place with 317 unicorns and the EU is a distant third with around 100 unicorns across the various member countries: UK (53), Germany (30) and France (26), according to PitchBook.

Europe has fallen badly behind the US in the technology race, while China in particular is rapidly catching up, and in some places has already overtaken Europe.

From the world's 100 most valuable tech companies the US accounts for about 60% and includes such household names like Apple, Microsoft, Nvidia, Alphabet, Amazon, Meta and Tesla, a few of which are worth over $1 trillion. US tech firms are much more profitable and are ten times the size of European tech firms.

Coming later to the game, China is in second place with around 15-20% of the top 100, including major companies like Tencent, Alibaba and PDD Holdings (Pinduoduo).

The EU holds about 5% of the top 100 but has some notable names like ASML from the Netherlands and SAP from Germany, which are both also in the world's top 20 most valuable global tech companies. Taiwan-based Taiwan Semiconductor Manufacturing Company (TSMC) should also get a special mention, as it dominates the world of very small and highly sought after microchips.

"European firms are smaller and less profitable than US ones. Europe's lacklustre productivity growth and low R&D expenses mean EU firms are lagging behind US peers. The gap with US is most striking among tech firms, which are twice as profitable and ten times bigger in US," says Agathe Demarais, a columnist at Foreign Policy.

China has been pouring money into R&D to close the gap with the US and has already managed to overtake it in several sectors. Ford CEO Jim Farley travelled to China with his CFO John Lawler in 2023 for the first time since the pandemic. They tested an electric SUV from their Chinese joint venture partner Changan and after thrashing it around a test track, Lawler turned to his

> "European firms are smaller and less profitable than US ones"

boss and said: "Jim, this is nothing like before. These guys are ahead of us."

The US has tried to protect its technological lead with the Inflation Reduction Act and the CHIPS laws that effectively outlaws the export of advanced technology to China. The measure badly backfired. US export controls on technology exports to China have instead hurt US technology companies, and effectively catalysed a consolidation amongst Chinese tech companies that boosted innovation and competitiveness in China's technology sector, according to a report from the Federal Reserve Bank of New York. And China has gone from a net importer of US technology, to a net exporter of technology, according to the report.

Russia's progress in technology is much more mixed, but it basically remains stuck in second gear. There are flashes of brilliance like the rapid development and roll-out of the Sputnik V vaccine in 2020, the first and one of the most effective vaccines against the coronavirus that came as a complete surprise to observers.

In a follow-up, Russia says it has developed a promising vaccine against mpox at the end of August, which could potentially provide lifelong immunity against the disease. It also produces state-of-the-art military hardware and has rapidly innovated and produced new high-tech drones and electronic warfare (EW) capabilities over the last two years, overtaking Ukraine's early lead. And Russia's nuclear power technology is world class.

But in other sectors is badly behind. As *bne IntelliNews* reported, it is at least two generations behind the West in the production of precision tools, with little chance of being to catch up any time soon. While the US leads the world on microchips with a well-established 7 nanometre microchip and is chasing a 4nm chip, followed by China that recently commercially produced a 7mn chip, Russia is stuck at the level of a 90nm chip – a brick by comparison. However, the Kremlin is throwing itself at innovation and pouring investment into other directions where it has some prowess, such as software and cyber technology, as part of its National Projects 2.1 programme.

The Kremlin is well aware the current strong growth is temporary so it has finally launched a campaign to modernise the economy both at the public and private levels as well as build up the military industrial complex. Putin told the heads of Russia's six military districts in May that the country needs to focus on both guns and butter when formulating its long-term economic development plans, enshrined in the updated National Projects 2.1 programme.

Russian companies have also been investing heavily in retooling their production lines to deal with the realities of sanctions. Investments in fixed capital in Russia moved up by 14.5% y/y in the first quarter of 2024, RosStat reported, to RUB5.93 trillion ($66.2bn) over the reported period. Fixed capital investments as of 2023 year-end gained 9.8% y/y and amounted to more than RUB34.04 trillion ($379.6bn). Like the US tech sanctions on China, the Western sanctions on Russia have spurred a period of investment and consolidation that has improved the productive health of the economy. Ironically, the flood of spending and investment has also undone some of the country's legendary income inequality as Russia's poorest regions have been the biggest winners from the changes.

Draghi's solution

The outlook for Europe to retain its competitiveness looks bleak but the Draghi report holds out some hope if drastic action is undertaken. The report identifies three main areas for action to reignite sustainable growth.

- **Close the Innovation Gap with the US and China:** Europe lacks dynamic new companies and invests significantly less in research and innovation than the US, particularly in advanced technologies. The focus needs to shift from mature industries like automotive to emerging sectors, and regulations must be improved to facilitate the commercialisation of innovations.
- **Coordinate Decarbonisation with Competitiveness:** High energy costs in Europe threaten industrial competitiveness. The EU leads in clean tech, but without a cohesive strategy to manage energy prices and align decarbonisation with growth, Europe risks falling behind, particularly with increasing competition from China.
- **Enhance Security and Reduce Strategic Dependencies:** Europe's reliance on external suppliers, especially for critical raw materials from China, poses risks to its security. A stronger EU foreign economic policy, including trade agreements, stockpiling and industrial partnerships, is needed, along with better coordination within the fragmented European defence industry.

And all this comes with a hefty bill: Draghi proposes a €800bn a year industrial makeover – more money than was spent on rebuilding Europe after WWII. He also warns there are several impediments to overcome before the plan will work.

"First, Europe is lacking focus. We articulate common objectives, but we do not back them by setting clear priorities or following up with joined-up policy actions," Draghi says, adding that overregulation and fragmentation are a major headache.

"Second, Europe is wasting its common resources. We have large collective spending power, but we dilute it across multiple different national and EU instruments," Dhragi went on. "Third, Europe does not coordinate where it matters. Industrial strategies today – as seen in the US and China – combine multiple policies, ranging from fiscal policies to encourage domestic production, to trade policies to penalise anti-competitive behaviour, to foreign economic policies to secure supply chains. In the EU context, linking policies in this way requires a high degree of coordination between national and EU efforts. But owing to its slow and disaggregated policymaking process, the EU is less able to produce such a response," adding it typically takes Europe 19 months to agree a new law. ●

European Commission President Ursula von der Leyen announces her commissioner proposals. / europa.eu.int

Eastern EU members secure key portfolios in new European Commission

bne IntelliNews

Several eastern European Union member states have secured important portfolios in the new European Commission, according to the nominations outlined by Commission President Ursula von der Leyen on September 17.

The newer EU members from Central and Southeast Europe are becoming increasingly assertive as they celebrate 20 years since the first wave of new members from the region joined the bloc, and 11 years since Croatia became the latest addition.

Von der Leyen referred to this when announcing the nominations, saying that of the six executive vice-presidents, "Three [are] from member states that joined before the fall of the Iron Curtain. And three from member states that joined after Europe was reunited. From the Baltics, Nordics and Eastern Europe. Ministers and prime ministers. Different backgrounds. But all with one common goal – and that is to make Europe stronger."

Key appointees from the region include Estonia's Kaja Kallas, taking the foreign affairs and security portfolio, and Lithuania's Andrius Kubilius, who will assume the newly created position of defence commissioner.

Kallas, Estonia's former prime minister, will succeed Josep Borrell. Known for her vocal stance on EU security, she had previously warned European leaders of a possible Russian attack on Ukraine.

"We are in an era of geostrategic rivalries and instability. Our foreign and security policy must be designed with this reality in mind and it must be more aligned with our own interests. I know that I can count on her to bring all of this together – and be the bridge between our internal and external policies. And to ensure we stay a Geopolitical Commission," said von der Leyen on announcing Kallas' appointment.

Kubilius' appointment as the first defence commissioner reflects the EU's focus on strengthening military manufacturing capacity in response to Russian aggression in Ukraine.

In a somewhat surprising move Romania's Roxana Minzatu has been appointed as one of six vice presidents, following Bucharest's efforts for a more prominent economic portfolio, though it ultimately secured a position focusing on people and skills.

Slovenia's Marta Kos is expected to take the enlargement portfolio, but her nomination remains under debate within Slovenia, with opposition parties fiercely contesting her candidacy.

Enlargement is expected to be a key focus for the next European Commission term, with Kos – should her appointment be approved – tasked with supporting Ukraine and assisting candidate countries in their preparation for accession.

Poland's Piotr Serafin has been entrusted with overseeing the EU's budget, a critical role within the bloc's financial framework.

Latvia's Valdis Dombrovskis and Croatia's Dubravka Suica, meanwhile, take less prominent posts than previously. Slovakia's Maros Sefcovic remains a key figure in the new Commission with his role in trade and economic security.

The European Commission is responsible for actions such as proposing new laws for the EU, approving or blocking company mergers and signing free trade agreements. Each member state has a representative in the new Commission, but their level of influence varies depending on the portfolio.

The bloc's biggest states, France and Germany, secured top jobs within the Commission, with von der Leyen herself being German and France's outgoing foreign minister Stsphane Sejourne taking charge of the industrial strategy portfolio.

The Commission's lineup includes 11 women, a figure falling short of the gender balance von der Leyen aimed for. "When I received the first set of nominations and candidates, we were on track for around 22% women and 78% men. That was unacceptable. So I worked with the Member States and we were able to improve the balance," commented von der Leyen.

Among the other notable appointments from the eastern EU members, Jozef Síkela of Czechia takes on international partnerships, Ekaterina Zaharieva of Bulgaria will handle startups, research and innovation, and Suica will manage the Mediterranean portfolio.

The new European Commission is expected to assume office by the end of the year, with one of its early tasks being to navigate the aftermath of the US presidential election in November, which could significantly impact EU-US relations, especially in light of potential shifts in the Western stance on supporting Ukraine.

All nominees will undergo hearings in the European Parliament, where lawmakers can challenge and block the nominees. ●

Czechia invites Israeli minister on international arrest warrant for a visit

Albin Sybera

Czech Minister of Defence Jana Cernochova has invited to Prague her Israeli counterpart Yoav Gallant, against whom the International Criminal Court (ICC) has issued an arrest warrant in connection with the actions of Israeli Defence Forces (IDF) actions in Gaza.

Czechia is a signatory country of the Rome Statute of the International Criminal Court and Czech police should arrest Gallant if he arrives in the country.

The Czech cabinet is a staunch backer of the far-right cabinet of Israeli Prime Minister Benyamin Netanyahu in its bloody campaign in Gaza but the invitation will put it in a difficult position, highlighting its break with the majority opinion of the international community.

Czech Ministry of Defence spokesperson David Polak confirmed for the online news outlet Aktualne.cz the "invitation for a personal visit of Czechia" for Gallant while Israeli embassy spokes-person Petra Mohylova said that "if the situation permits then such a visit could take place".

"Israel is a reliable partner and ally of Czechia. Mrs. Minister last talked with the Israeli minister over the phone last Thursday,“ Polak was quoted as saying.

Aktualne.cz also noted that while Prime Minister Petr Fiala's hawkish national security advisor Tomas Pojar ruled out Czechia would abide by the Rome Statute in the case of Israeli officials, the Czech Minister of Foreign Affairs Jan Lipavsky stated that "the position of the Czech government is that we abide by international law".

Cernochova hails from the neoliberal ODS party just like Fiala, which is also a more Eurosceptic party than Lipavsky's pro-EU Pirate Party.

Fiala also diverged from Czech diplomacy when he maintained the stance of the Czech pro-Kremlin ex-President Milos Zeman and called on the Czech embassy last autumn to be moved from Tel Aviv to Jerusalem.

Fiala also maintains a pro-Ukrainian stance and backs the arrest warrant issued by ICC against Vladimir Putin and other Kremlin officials.

News of Cernochova's invitation of Gallant to Czechia came as the United Nations condemned Israel's "blatant disregard" for international law in the Palestinian territories.

In the latest development, ICC Prosecutor Karim Khan called in Pre-Trial Chamber I of the court to issue arrest warrants against Gallant and Netanyahu as well as against Hamas leaders Yahya Sinwar and Mohammed Deif. Netanyahu described the effort as a "moral disgrace of the first order," *Times of Israel* wrote on September 10.

Over 1,000 Israelis, mostly civilians, were massacred by Hamas in October last year before IDF launched an air and ground offensive in the Hamas-controlled Gaza Strip which has so far claimed the lives of over 40,000 Palestinians, overwhelmingly civilians, according to figures released by the Hamas-run health authorities. ●

Poland says Germany's border controls "unacceptable"

Wojciech Kosc in Warsaw

The decision by the German government to introduce tighter border controls as measure to curb migration is "unacceptable," Poland's Prime Minister Donald Tusk said on September 10.

The apparently temporarily tightened border control regime kicks in on September 16, including along the nearly 500-km long Polish-German border. The border is an internal EU border covered by the free movement regulations, commonly known as the Schengen rules.

Poland watches over hundreds of kilometres of the EU's external borders with war-torn Ukraine and hostile Belarus and Russia. Those borders should be Germany's focus, Tusk said.

"What Poland needs is not a strengthening of controls on our border [with Germany], but a strengthening of the participation of states, including Germany, in guarding and securing the external borders of the EU," Tusk told a press briefing in Warsaw.

"It is the internal, political situation in Germany that is causing these steps to be taken and not our policy towards illegal migration at our borders," Tusk also said.

The PM thus referred to the political situation in Germany after an attack - claimed by a Syrian asylum-seeker on a festival in the town of Solingen that left three dead.

The anti-immigration rhetoric helped the far-right Alternative for Germany (AfD) party to win the regional vote in Thuringia and come runners-up in Saxony at the beginning of September.

While all of Germany's borders are internal borders of the EU falling under Schengen rules, the same rules make it possible to tighten controls temporarily to boost security.

Tusk also said Poland will seek consultations with Germany's neighbours on whether Berlin's decision should elicit a reaction from the EU.

Poland itself had instituted temporary controls along its border with Slovakia, citing the need to combat illegal migration along the so-called Balkan route, where migrants try to enter the EU from the non-EU countries such as Serbia through member states Hungary and Slovakia.

In what might be a sign of cooling Polish-German relations, Tusk also cancelled his trip to Germany, where he was due to receive an award for his pro-democratic and media freedom stance.

The spat over border controls also comes in the wake of Germany's pointing to Poland as a key actor in sabotaging the Nord Stream pipeline in September 2022.

Poland has recently told Germany to "apologise and keep quiet" about Nord Stream, which Poland says was the central element of Russian influence in Germany and the EU, and refused to hand over a Ukrainian suspected of direct involvement in the attack on the pipeline. ●

Donald Tusk (left) with German Chancellor Olaf Scholz earlier this year. / bne IntelliNews

Slovak Prime Minister Robert Fico has moved fast this summer to capture state institutions, including the judiciary, prosecution service and police. / bne IntelliNews

EU mulls sanctions against Slovakia over rule of law backsliding

Albin Sybera

The European Union is considering freezing some EU funds for Slovakia in response to the rule of law backsliding under the incumbent left-right cabinet led by populist Prime Minister Robert Fico, according to media reports.

Bloomberg wrote on September 8 that the European Commission could freeze part of the €12.8bn allocated for Slovakia from the EU's Cohesion funds, referring to its sources in the EC. The EC could also "claw back" the €2.7bn from the COVID-19 Reconstruction funds in response to government changes to the criminal code, which included reducing penalties for corruption, as well as changes to the prosecutor system that Brussels fears could make fighting corruption harder and potentially put EU funds at risk.

As part of these changes, the cabinet dismantled the Special Prosecutor Office overseeing high-profile corruption cases in which several officials linked to Fico's Smer party were caught up in the investigations and which also involved possible misuse of EU funds. The dismantling sparked country-wide protests and a constitutional challenge filed by previous liberal President Zuzana Caputova.

Bloomberg also noted that up to 80% of the public investments in Slovakia come from EU funds, adding that Slovakia would only be the second EU member country after Hungary against which the EU takes such action.

Slovakia's Minister of Foreign Affairs Juraj Blanar slammed Bloomberg for the reporting, saying that the "Slovak republic refuses the spreading of untrue information by *Bloomberg* agency about the suspension of EU funds for Slovakia." Blanar's ministry stated it has no information about EU action from its communication with the EC.

Slovakia's state broadcaster STVR quoted EC's response to its inquiry regarding the measures in which the EC stated that "only one case" – Hungary – is addressed in this way and that "at present, we don't have any other case, we should report on".

EC's spokesperson Veronica Favalli added that the EC is ready to take the necessary measures to block the EU funds if needed and that Slovakia met the May 15 milestone regarding the "fight against corruption and strengthening of integrity and independence of the judiciary" [...] "at the time of preliminary evaluation".

Fico's cabinet continued with sweeping staff changes at public institutions last month, which included firings at the country's key cultural institutions, a staff makeover at STVR, following the cabinet-backed restructuring of the public broadcaster, and dismantling of the elite police unit NAKA, which reportedly affected some 700 policemen.

Editor-in-Chief of the leading Slovak daily *SME* Beata Balogova wrote in her commentary on September 10 that "today not even [Hungarian strongman] Viktor Orban would get away with such intervention", referring to the way Boris Susko, Minister of Justice, intervened for the release of ex-prosecutor Dusan Kovacik from jail, where he was serving an eight-year sentence for accepting bribes from the mafia and shielding its members from criminal investigations during Fico's previous stint in power.

In the latest development, a court ended the criminal prosecution of the interim Chairman of the Parliament Peter Ziga of the centre-left Hlas party, who was indicted by police for bribing a judge of the country's Supreme Court in 2016. The case is now muted under the new statute of limitations under the criminal code, online news outlet Aktuality.sk wrote on September 10, quoting a confirmation from the spokesperson of the Prosecutor General Office Zuzana Drobova.

Peter Ziga has denied any wrongdoing, describing the indictment as "political games", Aktuality.sk noted. ●

In Erdogan's thinking, there is no need for Turkey to make its mind up one way or the other. / Nevit Dilmen, cc-by-sa 3.0

Turkey will deepen ties with East while facing West, says Erdogan

bne IntelliNews

Nato member Turkey will not stop deepening ties with the East, including the BRICS group of nations and the Shanghai Cooperation Organisation (SCO), but at the same time it will continue to face West, the country's president, Recep Tayyip Erdogan, was reported as saying at an event in Ankara on September 18.

Erdogan stated that debates over Turkey going through an "axis shift" were unfounded, but that Turkey had to adapt to new "centres of power" in terms of economies, production and technology, while ensuring it remained open to potential presented by every structure and actor, *Reuters* reported.

"That is the approach that lies behind our country's will to expand the basis of dialogue with all of them, from the Shanghai Cooperation Organisation to BRICS and Asean," Erdogan was quoted as adding.

And he said: "Of course, our face is turned to the West, but this certainly does not mean that we will turn our backs on the East, that we will ignore the East, or not improve our ties with the East."

The National Interest on September 17 published an opinion piece headlined "Turkey: A Ship Headed Eastwards", written by Robert Ellis, an international advisor at RIEAS (Research Institute for European and Amerian Studies) in Athens.

Ellis noted that Erdogan said in a speech four years ago: "Turkey has the political, economic and military power to tear up the immoral maps and documents imposed on it."

Suggesting Turkey always sets out to have its cake and eat it, Ellis concluded: "There seems to be no limit to Turkey's cakeism."

A BRICS summit in Kazan, Russia, to be held in October, is set to evaluate Turkey's BRICs membership application, as well as an application from Ankara's close ally Azerbaijan. The club of emerging nations is made up of its five original members Brazil, Russia, India, China and South Africa and four members who joined earlier this year, namely Iran, the United Arab Emirates, Ethiopia and Egypt.

In June, Turkish Finance Minister Mehmet Simsek, during a talk at London's Chatham House think tank, described BRICS as "a dialogue platform" compared to a formal economic bloc such as the EU.

"The EU remains our core partner in terms of trade investments, tourism flows ... so we remain focused [on the EU], but that doesn't mean we do not look at alternatives if they present value," he told the forum.

Asli Aydintasbas, a visiting fellow at the Brookings Institution's Center on the United States and Europe, this week told *VOA Mandarin* that "Turkey's BRICS bid is one more example of the country's drift away from the Transatlantic community".

"BRICS membership may not mean much in practical terms and Turkey is still keen to retain its Nato membership. But it is gradually, inch-by-inch, drifting from the West – and that requires greater strategic thinking on the part of US and other Nato allies, given Turkey's regional heft and geographic location. Is this an outcome we want?" said Aydintasbas.

Earlier this week, Turkey's move for BRICS membership hit a bump in the road when Russian economist Sergey Glazyev expressed opposition to it joining, arguing that Erdogan's stance that Russia should return annexed Crimea to Ukraine is "unacceptable".

Last week, Erdogan was reported by Turkey's state-run news provider *Anadolu Agency* as affirming in a video message to the Fourth Crimea Platform Leaders Summit held on September 11 that the "return of Crimea to Ukraine is a requirement of international law."

Prior to his reaction to Erdogan's comments on Crimea, Glazyev published an article titled "Türkiye has no place in BRICS."

In it, he said that in this period when the world economy is shifting to Southeast Asia, Russia is searching for allies further afield in Asia. Turkey and Azerbaijan, he said, were ideologically weak.

He said Moscow should even consider breaking off diplomatic relations with Turkey if Erdogan did not withdraw his comments on Crimea.

Erdogan's lavish Ankara, summer and winter palaces sting Turkish taxpayer for three billion lira

Akin Nazli in Belgrade

Turkey's president, Recep Tayyip Erdogan, has spent as much as Turkish lira (TRY) 3.3bn on building three palaces for himself, according to a Turkish daily.

Birgun newspaper reported on the cost to the public purse as Erdogan ordered the building of the Ankara presidential palace, a summer palace and a winter palace.

Converting the expenditure using the current exchange rate of 1 USD = TRY 34, the sum spent on the three palaces equals $97mn.

However, when the construction of Erdogan's first palace, located in Ankara's Bestepe district, kicked off in 2012, the exchange rate stood below TRY 2.0. The rate rose above the 2.0-level when Erdogan moved into the palace in 2014.

Turkey's strongman in 2015 launched, and lost, a legal action after a furore over whether his Ankara palace has gold-plated toilet seats. His lawyers pursued what they said were baseless allegations made by the then Republican People's Party (CHP) chief, Kemal Kilicdaroglu. Kilicdaroglu contended that he only made comments that were intended as a general criticism of officials' lavish lifestyles.

The Bestepe palace was built on a land plot within Ataturk Orman Ciftligi (AOC, or Ataturk Forest Farm), established at the request of the founder of the Republic of Turkey, Mustafa Kemal Ataturk, in 1925.

It has more than 1,000 rooms and officially cost TRY 1.37bn. The opposition, however, has claimed a total of TRY 4.86 has actually been spent on the palace.

You can take a virtual tour in the Bestepe palace here.

Erdogan's summer palace is on Okluk bay in the town of Marmaris in Mugla province on the southern Aegean coast. The cost of the Okluk palace, which has more than 300 rooms, was updated to TRY 725mn in the 2024 Presidential Investment Programme from TRY 686mn in the 2023 programme.

The construction of the Okluk palace started in April 2017, when the USD/TRY rate stood in the 3.00s. The exchange rate stood in the 5.00s when the palace was opened in 2019.

Media reports have outlined claims that sand from Lake Salda was transported to Okluk for use in improving the palace beach. Lake Salda, located in Isparta province, neighbouring Mugla, was a wonder of nature. Not anymore.

Finally, Erdogan built a winter palace in the town of Ahlat in the eastern province of Bitlis. The construction of the landmark was launched in 2019. The palace opened in 2020.

The cost of the Ahlat palace, the creation of which is scheduled for completion in 2026, has been updated to TRY 1.22bn.

Serbian President Aleksandar Vucic and Montenegrin President Jakov Milatovic at the Western Balkans' EU Ascent panel at Globsec in Prague. / Globsec

Enlargement fatigue and the Western Balkan security vacuum

Clare Nuttall in Glasgow

Top politicians from the Western Balkans confronted the question of when countries from the region can realistically hope to join the European Union at the Globsec forum in Prague.

There are fears that the protracted accession process – albeit speeded up somewhat since Russia's invasion of Ukraine – will lead local populations to become increasingly disillusioned with the EU, and create room for Russia and other parties to expand their influence in the region.

In contrast to fellow politicians from the region, Montenegro's President Jakov Milatovic was highly optimistic about his country's accession prospects. He pointed out that Montenegro is in the final phase of its EU accession process and could become the 28th member state by 2028. Although ambitious, he argued that this goal is realistic, citing Montenegro's long-standing use of the euro, its Nato membership since 2017, and its alignment with EU foreign and security policy.

Milatovic expressed hope that Montenegro's progress could serve as a catalyst for the entire Western Balkans region, stressing that regional cooperation and economic integration are key to securing the region's future within the EU.

Still, even Milatovic acknowledged the slow accession progress – no country has joined the EU since Croatia in 2013 – saying that what "we thought would be a 400m race ended up being a marathon with hurdles."

Speaking on the same panel as Milatovic, Serbian President Aleksandar Vucic was more sceptical, suggesting that no new EU members (even Monte-negro) would be admitted before 2030. Vucic acknowledged the desire of all Western Balkan countries to join the EU but warned that enlargement fatigue within the EU itself, compounded by the acceleration of Ukraine and Moldova's accession, could slow the region's progress even further.

"Everyone sees opportunities, a revival of the process, but I don't believe it. I wish all the best to Montenegro, but I do not believe that it will be part of the EU in 2028, and I do not believe that we will be a member in 2028, Vucic said.

"We all want to be part of the EU, but we are not sure what the situation will look like in the member countries. Ukraine and Moldova are gaining momentum, which is understandable, but at the same time there is public exhaustion within the EU regarding enlargement," the Serbian president added.

North Macedonia's President Stevo Pendarovski echoed these concerns, noting that his country, once seen as a frontrunner for EU membership alongside Croatia, has fallen far behind. It is now 19 years since the country secured candidate status, but its progress has been blocked by bilateral disputes with its neighbours, first Greece and later Bulgaria.

Pendarovski pointed to the EU's lack of commitment as a significant factor in the region's stagnation. Over the last 11-12 years, no country from the Western Balkans has made significant progress toward EU accession, and this has caused public enthusiasm for the EU to plummet, he argued.

In North Macedonia, for example, less than 50% of the population now supports EU membership – a shockingly low number for a historically pro-European country.

By contrast, Albanian Prime Minister Edi Rama told a panel that Albanians "are European, we are stubbornly in love with Europe" – a sentiment that is backed up by surveys showing Albanians are along the most enthu-siastic in the region about joining the bloc. However, he warned that "the Western Balkans should not be taken for granted".

With enthusiasm for enlargement faltering both in the EU and in parts of the Western Balkans, former Croatian president Kolinda Grabar-Kitarovic warned of the potential for a dangerous political vacuum to emerge. The lack of momentum threatens to destabilise the region and open it up to foreign influence, particularly from Russia.

Grabar-Kitarovic compared her country's sometimes slow and frustrating path toward EU membership – Croatia joined in 2013 – to the experience of the aspiring members from the Western Balkans today. She noted that Croatia's stalling progress on reforms impacted public support for EU accession, with similar trends visible today in neighbouring countries. She said that "enlargement fatigue" is nothing new, but the current situation is even more concerning.

As the process of EU accession stalls, political vacuums are emerging in the Western Balkans, which are being filled by third-party actors – particularly Russia. Grabar-Kitarovic warned that Russia's interest in the region could be seen as an attempt to open another geopolitical front, diverting attention from the war in Ukraine. She stressed that enlargement fatigue must be tackled through better public diplomacy to showcase the benefits of EU membership for both the candidate countries and the Union itself.

Rama argued that "the biggest promoter of expansion over the past two years ... wasn't [French President] Emanuel [Macron], it was [Russian President] Vladimir [Putin] and this is the tragic optimism unfortunately because Europe needed Vladimir to attack Ukraine so that it no longer takes for granted that the Western Balkans is there".

While pointing out that Albania has historically had less contact with Russia than any other country in Europe, he warned: "The region is a space where Russia has a lot of influence and before it's too late, we need to do some things differently". He welcomed steps from the EU's side, specifically the New Growth Plan to support integration of aspiring members with the bloc's economy.

Montenegro's former president Milo Djukanovic voiced similar concerns, highlighting the negative effects of the protracted accession process. He argued that the delay has resulted in public disillusionment, with many questioning whether EU membership is still a feasible goal. Đukanović remarked that in Montenegro, and throughout the Western Balkans, there remains a sharp divide between the vision of a multi-ethnic democracy and the lingering pull of Balkan nationalism.

Djukanovic also pointed out that the West's historical mistakes in dealing with the Western Balkans have created space for the resurgence of retrograde political ideas, such as the desire for ethnically homogeneous states. He further warned that Russian influence in the region seeks to exploit these divisions, undermining stability and threatening to push the region back into turmoil.

The contrasting perspectives at Globsec highlighted the region's deep frustration with the EU enlargement process. Enlargement fatigue threatens not only the prospect of EU integration but also the stability and security of the Western Balkans as a whole. as pointed out by several politicians at Globsec, Without renewed commitment from both the EU and the Western Balkans, the region risks becoming increasingly vulnerable to external influence and internal instability." ●

B9 Nato countries call for integrated air defence system to address Russian threat

Iulian Ernst in Bucharest

The Nato countries forming the Bucharest Nine (B9) format, meeting in Romania's capital city on September 18, called for a "joint air defence" system in response to the Russian "slow flying objects" (drones) that are increasingly violating allied airspace during attacks against Ukraine.

"This is a new reality that cannot be left disregarded. We need a collective answer within Nato to challenges posed by modern weapons and technologies including through boosting our capabilities of detecting, identifying and, if necessary, engaging low and slow flying objects," a joint statement from the B9 countries published by Romania's defence ministry said.

"The B9 states are deeply concerned about the repeated incursions of Russian drones and missiles into Nato airspace in Poland, Romania, and Latvia, as well as the escalation of tensions along Nato's borders," Romanian Defence Minister Angel Tilvar said, quoted by *Kyiv Independent* during a press briefing after the B9 meeting in Bucharest.

The B9 signatories called for the consolidation of Nato's integrated air defence system in the region and for the "fastest possible" implementation of the system through rotation in this regard.

"We support initiatives to utilise all available opportunities and resources within the EU and Nato to increase European air and missile defence capabilities. We reiterate the need for Russia's full compliance with international law, including the inviolability of Nato airspace," the statement reads.

The B9 format includes nine Central and Eastern European members of Nato and the EU: Bulgaria, Czechia, Estonia, Hungary, Latvia, Lithuania, Poland, Romania and Slovakia. ●

Croatian President Zoran Milanović at a recent event marking the 30th anniversary of the founding of the 20th Home Guard Regiment in Glina. / predsjednik.hr

Croatian president in new row with government for using army helicopter "like a taxi"

bne IntelliNews

Croatian President Zoran Milanovic is facing a backlash over his use of military helicopters, igniting a fresh political conflict with Prime Minister Andrej Plenkovic's government. The issue, which has sparked a debate about the misuse of military resources, comes as the Ministry of Defense estimates the flights have cost taxpayers at least €1mn.

The row is the latest in a series of stand-offs between Milanovic, backed by the opposition Social Democratic Party (PSD), and Plenkovic's ruling Croatian Democratic Union (HDZ). The acrimonious relationship between Milanovic and the government has intensified as the December presidential approaches. That will pit Milanovic, who is seeking re-election, against the HDZ's candidate Dragan Primorac.

The controversy escalated after reports surfaced that Milanovic had flown military helicopters 348 times during his presidency, including to popular destinations such as Hvar and Brijuni.

Defence Minister Ivan Anusic criticised the president's frequent use of military resources, and claimed the president "misled the public and made untrue claims" regarding his use of these aircraft.

According to Anusic, the 348 flights, totalling 241 flight hours, were conducted at Milanovic's request, at a cost of at least €1mn. He detailed that 90 flights were made using Black Hawk helicopters, 120 with Mi-8 MTV helicopters and 138 with Mi-171 Sh helicopters, all of which accumulated significant expenses.

The Office of the President, however, pushed back on these figures, reporting that Milanovic had used a military helicopter only 74 times and a military ship eight times since February 2020, with fuel costs amounting to €127,000 for the Croatian Air Force and €22,800 for the Croatian Navy. A statement from Milanovic's office described additional claims as "manipulations" and "completely inaccurate data".

In response, Anusic argued that the fuel costs represented only a portion of the total expense, saying that the use of military resources for the president's travels diverted personnel and equipment from essential military training.

In his latest comment on the issue on September 3, Anusic challenged Milanovic's account, saying that 348 helicopter flights had been made in response to the 74 orders from the presidency.

"[A]s the Minister of Defence I am responsible for the transparent spending of money and resources of the Armed Forces ... In my opinion, that is too much, the cost is over €1mn," he said, according to a government statement.

He called again for Milanovic to publish a report on where he flew in Armed Forces helicopters and what state affairs he did.

As the row intensified, Plenkovic accused Milanovic of treating military resources like a personal taxi service.

> "Croatia did not buy Black Hawk helicopters to use them like a taxi. I do not see any of the rest of us using the army's resources so nonchalantly"

"Croatia did not buy Black Hawk helicopters to use them like a taxi," Plenković told reporters, adding that military resources are not intended for casual use. "I do not see any of the rest of us using the army's resources so nonchalantly."

Milanovic has now ordered the military secret service (VSOA) to investigate leaks from the Ministry of Defence regarding his helicopter flights, which he claimed posed a threat to national security. Milanovic expressed frustration after national television cameras filmed his helicopter landings on two occasions, prompting him to question how journalists were informed of his movements.

In a retaliatory strike, Milanovic criticized Plenkovic for using government planes, which he claimed were "10 times more expensive".

On September 4, the president took to Facebook to criticise Anusic. He claimed to previously have had a good relationship with the defence minister until the current row, saying the current

"I would therefore like to hear from the minister; what has changed in the last month? I can only guess and somehow it seems to me – and I am not the only one – that Minister Anusic's dissatisfaction with our cooperation coincides somehow with the beginning of Mr. Primorc's campaign," Milanovic wrote on his Facebook page.

"And this can only mean that Minister Anusic also unquestioningly put himself at the service of Andrej Plenkovic."

The scandal has drawn widespread public attention, raising questions about the balance between the president's role as commander-in-chief and the government's oversight of military expenditures. It follows previous high-profile debates between Milanovic and the government over issues such as Croatia's stance on the Ukraine war and the actions of the right-wing Homeland Movement, the HDZ's junior coalition partner." ●

Bulgarians outraged after North Macedonia's deputy PM calls them "miserable"

Denitsa Koseva in Sofia

Bulgarian politicians were outraged when North Macedonia's Deputy Prime Minister Aleksandar Nikoloski called President Rumen Radev an "uncivilised host" and Bulgarians "miserable" in response to the recent escalation of diplomatic tensions between the two countries.

Earlier in September, during a meeting between Radev and North Macedonia's President Gordana Siljanovska-Davkova in Sofia, the flag of North Macedonia was absent, which angered Skopje.

Following Nikoloski's interview, the Bulgarian foreign ministry issued a statement, calling his words insulting, and his tone un-European and incompatible with good manners.

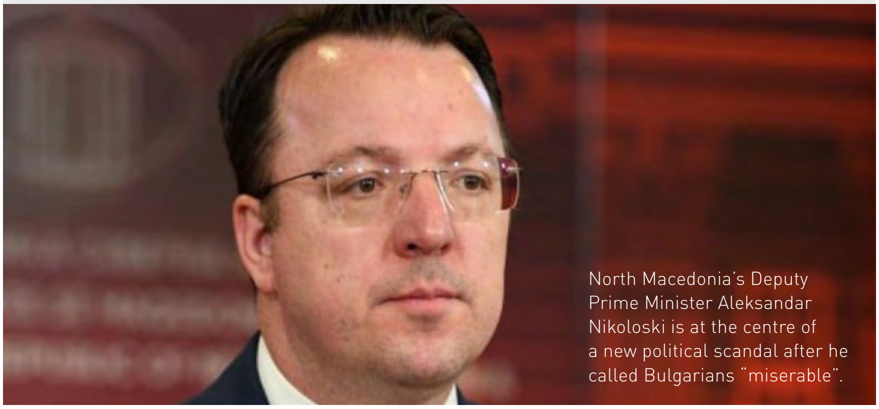
"Our partners have been notified of the unprovoked provocations, aimed, among other things, at destroying the dialogue. Once again, we recall the key importance of the development of good neighbourly relations for the European future of the Republic of North Macedonia," the ministry said in the statement.

Siljanovska-Davkova visited Bulgaria to attend a performance of Giuseppe Verdi's Nabucco by the Macedonian Opera and Ballet, which opened the new season at the Sofia Opera. The Macedonian delegation included Foreign Minister Timco Mucunski and Minister of Culture Zoran Ljutkov.

The president used her visit to Sofia to meet with her Bulgarian counterpart. The discussions were focused on resolving the long-standing tensions that have persisted since Bulgaria's veto of North Macedonia's EU accession talks in 2020.

Radev also reacted, suggesting that the informal meeting has bothered some circles in Skopje and saying that he had a constructive dialogue with Siljanovska-Davkova. He also pointed out that the visit of North Macedonia's president was not official and that he hoped Siljanovska-Davkova to soon pay a formal visit to the country.

Several political parties also called for an official reaction to Nikoloski's statement, saying it can blow up the good neighbourly relations.



North Macedonia's Deputy Prime Minister Aleksandar Nikoloski is at the centre of a new political scandal after he called Bulgarians "miserable".

As discussions of a potential "direct clash" between Russia and Nato in the Ukraine war grow, Belarus and Russia are finalising security agreements ahead of their joint military exercises, Zapad 2025 (West 2025), later this year.

Belarus and Russia strengthen security ties amid rising tensions

Leon Aris in Berlin

As the talk turns to a possible "direct clash" between Russia and Nato in the escalating Ukraine war, Belarus and Russia are tightening their mutual security agreements, with negotiations expected to conclude ahead of the annual joint military exercises Zapod 2025 (West 2025) later this year. These manoeuvres could serve as cover for the formation of a Russian-Belarusian strike group, reports *Belarus in Focus* September 15.

Belarusian Security Council Secretary Aliaksandr Valfovich said both nations are deepening military and political integration in a recent interview. The increasing presence of US and Nato forces near the borders of the "Union State" of Belarus and Russia has escalated tensions in Eastern Europe.

"Over 30,000 Nato troops are stationed in the region, with 20,000 deployed in Poland and the Baltic States," he said. A US tank battalion is also permanently positioned along the Lithuanian-Belarusian border, while Poland has mobilised 17,000 troops along its eastern frontier, according to Valfovich.

Nato's ongoing expansion – now including Finland and Sweden as members –further fuels Belarus and Russia's concerns. The Alliance is seen as pursuing the inclusion of Balkan countries and post-Soviet states, prompting Minsk and Moscow to enhance their security cooperation.

Since 2000, Belarus and Russia have operated the Regional Force Grouping and launched the Unified Regional Air Defence System in 2009. Joint military exercises and operations are ongoing, and Belarus is adjusting its military strategy based on Russia's experience in its "special military operation" in Ukraine. Valfovich noted the need to strengthen Belarus' military presence along the Ukrainian border due to "persistent provocations by Ukraine," including alleged airspace violations by Ukrainian drones. Despite this, Belarus continues to offer itself as a neutral venue for peace talks.

In the last three years, the Union State deal, agreed in 1999 but never completed, has updated key strategic documents, including the Military Doctrine and the Information Security Concept. A new Union State Security Concept is under development and will be signed in 2025. However, a treaty on security guarantees between Minsk and Moscow is expected to be finalised by the end of this year. Belarusian Foreign Minister Maksim Ryzhankou stated that this agreement will cover the use of nuclear and conventional weapons, providing Belarus with security assurances as the Union State braces for a possible escalation in the Russia-Ukraine conflict.

In the event of such an escalation, the possibility of a new invasion from Belarusian territory looms, potentially involving the Belarusian military and tactical nuclear weapons. Valfovich confirmed that Belarus is ready for the possible use of non-strategic nuclear weapons, with scenarios for their deployment practised in joint exercises with Russia.

Belarus has also confirmed that the Russian-Belarusian strategic exercises of the West Regional Force Grouping will take place in 2025. While specific dates have not been announced, past exercises suggest the active phase could occur in September, following the deployment of Russian troops to Belarus in the summer of 2025. There are indications that additional Russian forces could begin arriving as early as the end of 2024. Some analysts suggest the Zapod 2025 drills could follow the "Union Determination" model used in early 2022, potentially serving as a pretext for launching a new invasion of Ukraine from Belarus. ●

Navalny's team accuses Khordokovsky ally Leonid Nevzlin of orchestrating attack on Leonid Volkov

bne IntelliNews

The team of the killed Russian opposition figure Alexei Navalny has accused Russian-Israeli billionaire Leonid Nevzlin of orchestrating an attack on Navalny's ally, Leonid Volkov.

On March 12, Volkov, former chief of staff to Navalny and chair of the Anti-Corruption Foundation (FBK), was attacked outside his residence in Lithuania with tear gas and a hammer. The Polish authorities arrested three individuals in connection with the incident, while Lithuanian officials have suggested possible involvement by Russian special services. However, Navalny's team has claimed it has evidence implicating Nevzlin in the attack, as well as a number of other attacks on other Navalny allies, including FBK director Ivan Zhdanov and economist Maxim Mironov's wife, Alexandra Petrashkova.

Nevzlin is the former co-owner of Yukos, an oil company that was also owned by famous Kremlin critic Mikhail Khodorkovsky. Nevzlin left Russia for Israel in 2003, and set up a media empire in the country, which included the takeover of *Haaretz*, Israel's longest running newspaper currently in print. In May 2024, he renounced his Russian citizenship, famously calling the population "Russian slave cattle."

According to Navalny's team, Nevzlin allegedly ordered Volkov's kidnapping and beating. It is alleged that he then refused to pay the promised $250,000 after the attack, as Volkov had not been beaten up badly enough. This then led to a dispute, which eventually led to Navalny's team being told about the attack.

Maria Pevchikh, head of FBK International, reported that the Navalny team received an anonymous offer from someone who had details about the attack on Volkov. The offer came from a man named Andrey Matus, a middleman

On March 12, Volkov, former chief of staff to Navalny and chair of the Anti-Corruption Foundation (FBK), was attacked outside his residence in Lithuania with tear gas and a hammer. / Ivan Zhdanov

"The information also included other plans, including an initial scheme to kidnap Volkov in Lithuania and transport him to Russia"

with alleged connections to authorities. Matus, who claims to have worked for Khodorkovsky in the past, arranged a meeting with a number of members of FBK in Montenegro. At this meeting, Matus explained that he was responsible for retrieving the assailants' phones following the attack. During this meeting, he allegedly played a recording of his conversation with Nevzlin, which confirmed the details of the attack on Volkov and other opposition figures.

The information also included other plans, including an initial scheme to kidnap Volkov in Lithuania and transport him to Russia. However, this plan faltered, leading to a second attempt to attack Volkov in the US. Ultimately, Volkov was assaulted in Vilnius, suffering from multiple injuries. Despite the attack's completion, Nevzlin was reportedly dissatisfied with the results, expressing frustration over the severity of Volkov's injuries. This dissatisfaction led to accusations and counterclaims between Nevzlin and his associates, culminating in Matus seizing and handing over phones used in the attack organisation to FBK.

The situation then took a turn when Matus disappeared after learning that Navalny's team would not pay him for the evidence. Soon after, the same information surfaced on the Kremlin-supported Russia Today.

Nevzlin has strongly denied any involvement in the attacks, dismissing the allegations as unfounded and politically driven. He called for an independent investigation and expressed confidence that a fair judicial process would clear him of any wrongdoing. He accused Moscow of being behind the evidence. ●

Who is Ukraine's new Foreign Minister, Andrii Sybiha?

Ben Aris in Berlin

Ukrainian President Volodymyr Zelenskiy shook up his government on September 5 and replaced Foreign Minister Dmytro Kuleba with Andrii Sybiha, along with almost a dozen of other ministers and senior officials to "reinvigorate" his administration, the president said the next day.

Kuleba had held the post of Foreign Minister since March 2020 and worked tirelessly to rally support for Ukraine's existential war with Russia. However, as *bne IntelliNews* has reported, Kyiv has run up against a brick wall in recent months as Ukraine fatigue sets in and its Western allies have dragged their heels on providing both military and financial help. In particular, a G7 $50bn loan to Ukraine, approved on June 13 at a G7 summit in Italy, is caught up in wrangling amongst the partners over who is going to contribute how much. Germany recently announced it will scale down the amount it contributes in the coming years, leaving a $12bn hole in the 2024 budget that will rise to $15bn in 2025, according to recent statements by the Ministry of Finance (MinFin).

The second issue is Bankova's (Ukraine's equivalent of the Kremlin) increasing frustration with the US, which continues to block permission for Ukraine to use the powerful Nato-supplied missiles to hit targets deeper inside Russia that are badly needed to be struck following the Kursk incursion that began on August 4. According to recent reports, the defence of the front line in the Donbas regions is beginning to crumble, leading some to ask whether the invasion of Russia was a strategic blunder.

Sybiha takes over a big and difficult portfolio. A seasoned diplomat and former First Deputy Minister of Foreign Affairs, he was confirmed in his new job by the Rada with 258 votes, comfortably passing the required 226 threshold.

Sybiha's appointment comes as part of a broader reshuffle within the Ukrainian government, aimed at injecting "new energy" into its leadership. Zelenskiy, who had announced his intent to overhaul the administration the day prior, remarked that the changes were essential to bolster the country's capabilities in "international politics and diplomacy." He added: "We need new energy today."

A career diplomat

Sybiha was born in the western Ukrainian town of Zboriv in 1975, and rose steadily through the ranks of Ukraine's foreign service, reports *Vedomosti*. A graduate of the Ivan Franko National University of Lviv with degrees in international relations and law, he began his career at the Ministry of Foreign Affairs (MFA) as an attaché in the legal department.

Sybiha's foreign service includes two stints at the Ukrainian Embassy in Poland, first in the late 1990s and later from 2008 to 2012, where he served as an adviser-envoy. He is fluent in Polish and English, and maintains good relations with the Polish-Ukrainian community, and as he is part-Polish himself, he is seen as a natural interlocutor in relations with Kyiv's western neighbour.

Sybiha's diplomatic career also included stints as the head of Ukraine's consular service and as ambassador to Turkey between 2016 and 2021 – another key Ukrainian ally – where he helped establish a visa-free regime. His time in Ankara saw him forge strong ties with the Turkish authorities, and he has been vocal about Ukraine's strategic relationship with Turkey, reports *Vedomosti*. In an interview, he praised Turkey as "the only state in the world that agreed to supply attack drones to Ukraine during a very difficult period," referencing the crucial Bayraktar TB2 drones supplied to Ukraine at the start of the war.

"Sybiha has also taken a firm stance on Russia, regularly criticising Moscow's role in post-Soviet conflicts even before the war started"

Sybiha has also taken a firm stance on Russia, regularly criticising Moscow's role in post-Soviet conflicts even before the war started. In a 2020 interview with *Bloomberg Businessweek Turkiye*, he accused Russia of conducting a "hybrid information war" against Ukraine and manipulating history to claim victory over Nazism. He has also been a sharp critic of the Nord Stream 2 gas pipeline that was destroyed in September 2023, which he described in 2021 as "Russia's geopolitical weapon" and a threat to both European security and energy stability.

A key adviser to Zelenskiy

In May 2021, Sybiha moved from the MFA to the Office of the President, where he was appointed Deputy Head, focusing on foreign policy and strategic partnerships. His tenure coincided with the height of Russia's invasion of Ukraine, during which Sybiha was a key figure in organising international support for President Zelenskiy and coordinating diplomatic efforts abroad. He played a significant role in Zelenskiy's global engagements, including helping to craft the president's speeches during his visits to foreign capitals.

Sybiha grabbed the limelight in April 2023 when he announced Ukraine's planned counter-offensive against Russia in an interview with the *Financial Times*. He notably stated that Ukraine would be prepared to "open a diplomatic page" to discuss the Crimea once it had reached the peninsula's administrative borders but did not rule out a military option. His remarks were part of Ukraine's broader strategy to regain lost territory, which remains central to its military and diplomatic calculus as part of Zelenskiy's 10-point peace plan that was introduced at the G20 summit in November 2022.

Challenges ahead

As Sybiha steps into the role of foreign minister, he inherits a difficult portfolio. His predecessor, Kuleba, was instrumental in galvanising international support for Ukraine during

Ukraine's new Foreign Minister Andrii Sybiha is a career diplomat who has worked in Poland and Turkey, as well as helped organise the Swiss peace summit in July. He takes over a tough portfolio as Ukraine is under increasing military pressure and more dependent on Western help than ever. / bne IntelliNews the war, and Sybiha will now be tasked with building on that momentum as the military situation worsens.

One of his immediate responsibilities will be to navigate the complex diplomatic landscape surrounding Ukraine's peace efforts. Zelenskiy has called for a second peace summit in November to which China and Russia will be invited following the failure of the Swiss peace summit held on June 16-17 that was supposed to renew Ukraine's international support and further isolate Russia. However, only 76 countries signed off on the final watered down communiqué – half the number that voted to condemn Russia in the UN voting at the start of the war, highlighting the inroads Russia has made in undermining Ukraine's support amongst the Global South.

In his previous role, Sybiha helped organise Ukraine's Swiss peace summit, travelling to China in June 2024 to meet senior officials, including Sun Weidong and Li Hui, in an attempt to secure Beijing's participation, which failed. Beijing said that as long as Russia didn't attend the event China saw no point in attending. Nevertheless, Sybiha's experience in high-stakes diplomacy will be critical as Ukraine continues to seek international backing for its territorial integrity and post-war reconstruction.

Relations with Poland, a strong backer of Ukraine's effort to restore its territorial integrity, have been marred by a polemical trade row, after cheap Ukrainian grain wrecked the Polish grain market in April 2023, causing Warsaw to unilaterally ban the transit of grain to the EU – one of Ukraine's biggest foreign exchange earners. That ban remains in place and other disputes over Ukrainian truckers transiting the country have appeared in the meantime.

Sybiha took a combative stance towards Poland over its grain exports ban, where he accused Warsaw of pushing Ukraine towards "euthanasia" by prolonging an embargo on Ukrainian agricultural products.

Poland will continue military assistance to Ukraine for "as long as it takes," in line with a comprehensive bilateral security deal Zelenskiy announced following a meeting with Polish Prime Minister Donald Tusk in July. However, Tusk qualified the relationship saying that Poland would block Ukraine's membership of the EU unless it "owned up to past atrocities." The two countries have a long and troubled history, especially during WWII when Ukrainian nationalists partnered with the Nazis, which led to a massacre of 60,000 ethnic Poles living in western Ukraine that had been part of Poland in the past, amongst other things. Warsaw has long said that Ukraine should formally apologise for what it calls a genocide.

As Ukraine's new top diplomat, Sybiha will also likely focus on expanding Kyiv's ties beyond its traditional partners. Kuleba has recently toured SE Asia and Africa in an effort to drum up more support for his country in the Global South, particularly in the wake of the recent Swiss peace summit. The stakes are high as Ukraine continues to face Russia's aggression while striving for international recognition of its sovereignty over Crimea and the Donbas regions. ●

Tusk says Ukraine won't join EU without owning up to past atrocities

Wojciech Kosc in Poland

Polish Prime Minister Donald Tusk has said that Ukraine will not get Poland's consent to join the European Union unless it meets Warsaw's expectations on how it should deal with Ukrainian nationalists' World War 2-era atrocities against Poles.

Poland has been one of Kyiv's most dedicated allies since Russia attacked Ukraine in February 2022. Polish authorities have sent huge volumes of military equipment and welcomed hundreds of thousands of refugees.

Warsaw has long said that it is in Poland's best interest for Ukraine to stop Russia so that Poles do not need to fight the Russian army themselves on their home soil one day.

But Ukraine's sacrifice of blood for the sake of Poland's security is not going to set the two neighbours' complicated historical record straight once and for all despite Ukrainian officials hinting at exactly that.

It's not simply "history"

While on a visit to Poland, Ukraine's Foreign Minister Dmytro Kuleba said that history belongs to history now that Ukraine is struggling against Russian aggression.

"If we were to start digging into history today, the quality of the conversation would be entirely different, and we could go very deep into the past, bringing up the wrongs that Poles did to Ukrainians and Ukrainians did to Poles," Kuleba said.

The Ukrainian minister also said that the "focus should be on building the future together and leaving history to the historians".

The statement rubbed Poland up very much the wrong way.

"My assessment of what the Ukrainian minister said is clearly negative," Tusk said on August 30 , adding that Ukraine will have to "meet Poland's expectations, not so much about digging into history, but rather about shaping our relationship based on the truth of that history".

The Polish PM also said that "the EU wouldn't have come into existence without reconciliation between Germans and French or Germans and Poles".

"Ukrainians need to understand that joining the EU means entering a space with standards related to political and historical culture," Tusk also said.

Tragic ties

The often tragic history of Poland and Ukraine goes back several centuries. Before Ukraine's national identity began to be forged, the Ukrainian lands had been under Polish and Russian rule. Poles held the economic and cultural hegemony over the then-largely peasant Ukrainian population.

Ukrainians' inferior position in Poland – in the first republic that collapsed in the late 18th century and in the short-lived second republic that existed between the end of World War 1 and the outbreak of World War 2 – was an important driver of the nationalist movement, which was struggling to establish a Ukrainian state.

Unfortunately for Ukrainians, their efforts first came head-on against Poland's efforts to build a state after World War 1.

Later, when the Nazis invaded the USSR in 1941, some Ukrainian nationalists considered it a new opportunity to build a country in a sort of alliance with Hitler (who considered Ukrainian aspirations as nothing else but helpful tactics to employ against the Soviet Union).

The totality of World War 2 turned out conducive to Ukrainian nationalists' brutal crackdown on Poles living in Western Ukraine at the time. Historians estimate 60,000 Poles died in the killings that lasted with varying intensity between 1943 and 1945.

Despite the two nations now on their best terms in history – because of Poland's unequivocal support for Ukraine in the wake of the Russian invasion in 2022 – the atrocities remain a dividing point.

Poland considers the massacres genocide and has long said that Ukraine should formally apologise. But the wartime nationalist movement is an important part of Ukraine's history for its role in building its national identity, making it difficult for Kyiv to formally acknowledge its crimes.

Ukraine – as expressed by Kuleba – would rather delegate the debate on the atrocities to historians. That would be merely glossing over an important part of Polish history and doing the victims an injustice, Warsaw invariably says in reaction.

Apart from an apology, Poland demands that the killing sites are examined so that the remains of the victims are given a "dignified burial". Work is already underway on some sites.

Past and present

All that presents a political problem for the incumbent Polish government – just as it did to its predecessors.

Last week, Tusk made it clear that coming to terms with history will be as important for Ukraine as meeting the standard requirements of an EU membership.

"Ukraine will not become a member of the European Union without Poland's consent. Ukraine must meet various standards – this isn't just about borders, trade, or legal-economic standards. It also involves what I would call cultural-political standards," Tusk said.

In contrast, Szymon Holownia, the Polish parliamentary speaker and the leader of the Third Way, one of the parties making up the ruling coalition, suggested that he'd rather see Ukraine in the EU first.

"We will [discuss history] in the safe ecosystem in the EU when there is no killing in the streets by the dictator in the Kremlin," Holownia told the Globsec forum in Bratislava, Slovakia, last week.

"We won't solve the problems of the past if we mix it with Ukraine's position now," Holownia also said.

There is no shortage of present problems, either, related to the conditions on which Ukraine joins the EU one day (it took Poland over a decade to do that).

Polish truckers have long complained about cheap Ukrainian competition pricing them out of the EU market, for example.

But the real problem to solve will be agricultural subsidies and what will happen to Europe's agricultural and food businesses if Ukraine joins the bloc, gaining an unfettered and duty-free access to the market.

Ukraine would be entitled to a massive €186bn in subsidies if it joins the EU under current rules, or €16bn a year, more than Poland's €11bn a year.

Polish Prime Minister Donald Tusk addressing the audience during an event to commemorate the 85th anniversary of the beginning of World War 2. / Donald Tusk's office

The war in Ukraine has caused destruction and death and pushed Europe into recession, but it has been an economic and geopolitical windfall for most of Central Asia. / bne IntelliNews

Central Asia is a big winner from the Ukraine war

Ben Aris In Samarkand

The outbreak of war has caused devastation in Ukraine, major economic distortions in Russia that will doom it to long-term stagnation and sent Europe into recession as it starts to deindustrialise. But there is one group of countries that have done very well from the war: Central Asia.

Largely sitting on the fence, the five 'Stans – Kyrgyzstan, Uzbekistan, Kazakhstan, Tajikistan and Turkmenistan – have seen their trade volumes surge and demand from Russia, now cut off from traditional suppliers in Europe, is fuelling a manufacturing and investment boom.

But it hasn't been plain sailing. The countries of the Silk Road have been through some seismic changes in recent years, not limited to the war. Central Asia is also caught up in the growing tension between Washington and Beijing and the Taliban's return to power in Afghanistan, which is threatening the security of the region.

But even before the war in Ukraine started, most of the 'Stans were flourishing as three decades of economic reforms begin to pay dividends. Now the extra trade income and mushrooming demand is supercharging change, and they are ploughing the proceeds back into development.

The biggest change is the hundreds of millions of dollars of trade re-routed via one of the five 'Stans on its way to Moscow is by passing the extreme sanctions on Russia imposed by the West. But the bulk of the trade is not sanctions busting; simply the export of goods that Russia can't get due to self-sanctioning by Western firms that don't want to do business with Russia any more.

Kyrgyzstan in particular has seen budget revenues double in the last year and is using the windfall to invest into massively expanding its hydropower generation capacity to turn the small mountainous republic into an energy epicentre for the rest of the region.

But beyond that, nestled between east and west, with significant supplies of raw materials, oil and gas and rare minerals, Central Asia has become strategically important the rest of the world in a way that it has not enjoyed since the times of the Great Game.

Following the Russian invasion of Ukraine, many analysts believed that the 'Stans would be forced to choose sides or face sanctions. That didn't happen. What has emerged is a delicate multivector balancing act. In March 2022, then Uzbek foreign minister Abdulaziz Kamilov became the first Central Asian official who called for an immediate ceasefire in Ukraine, affirmed the sovereignty of that country, and refused to recognise Donetsk and Luhansk as independent republics.

The 'Stans have refused to recognise Russia's attack on Ukraine as legitimate. Face to face with Putin at St Petersburg International Economic Forum (SPIEF) in 2022, Kazakhstan's President Kassym-Jomart Tokayev refused to recognise Russia's claim that the breakaway republics in Donbas were independent. But at the same time the 'Stans abstained in the UN votes to condemn Russia in 2022 and have rebuffed Western pressure to halt the sanctions-busting trade they have facilitated since.

Wooed by Washington, Moscow and Beijing in an increasingly fractured world, the five 'Stans have clubbed together into the so-called C5 format to better leverage their stance in the negotiations.

"The war in Ukraine and Taliban control of Afghanistan did not isolate Central Asia; on the contrary, these events revitalised the region's relationships with major global powers. The region's leaders, acting as unified "C5" bloc, have visited Beijing, Berlin, Brussels, Moscow, New York and Xi'an. In turn, international leaders have made an unprecedented number of visits to the region. Russia's Putin visited all five Central Asian states in 2022 alone, China's Xi Jinping has toured the region twice since February 2022, Emmanuel Macron became France's second president to visit Central Asia, and Germany's Olaf Scholz is planning a trip to the region in September 2024," Jennifer B. Murtazashvili wrote in a paper for Carnegie entitled Nobody's Backyard: A Confident Central Asia.

Ironically, the East-West conflict and the pressure being applied to Central Asia to choose sides has led to an improvement in the region's relations with both East and West precisely because its countries' support of both sides is only partial, and even more importantly amongst themselves. The 'Stans have been prone to bicker in internecine rivalries for most of the time since their independence.

"Central Asian states have successfully deepened ties with international partners who are often at odds with one another. The region has avoided making binary choices and instead fostered an environment where even conflicting states can coexist. They have turned crises into opportunities for positive-sum cooperation," Murtazashvili said.

"What has emerged is a delicate multivector balancing act"

The international brouhaha has engendered an era of unprecedented co-operation amongst the normally fissiparous states. Indeed, the rivalries between the warring factions of East and West have liberated the 'Stans from the pressures that used to be exerted by the great powers that surround them.

"Observers predicted that these events would have severe effects on Central Asia's stability or destabilise long-standing regimes in the region. Although none of the catastrophic scenarios materialised, many still perceive Central Asia as a fragile region. What most analysis misses is the increased agency that countries in the region have over their own fates. The region is no longer a backdrop for the new Great Game, nor is it anyone's backyard," Murtazashvili said.

"Rather than cowering in fear and calling on larger powers to save them, Central Asian nations are exuding an independent confidence. Far from being passive or helpless players, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan are demonstrating that they are not pawns in a larger geopolitical game, but important actors who understand the leverage they have over larger goliaths. They are boldly and creatively tackling some of the world's most complex geopolitical tasks."

Business is booming

The trade with all of the countries of Central Asia and the Caucasus is booming thanks to the war. Cut off from direct imports of key inputs from Europe, much of that trade has simply been redirected via Central Asia, which has no qualms about dealing with banned goods. The trade has created a huge windfall for the 'Stans, money they are pumping into their economic development. Kazakhstan's imports of office machinery from Europe tripled to almost $1bn from 2021 to 2023, probably partly due to a surge of new offices and factories being set up to serve Russia's burgeoning demand.

Exports from the European Union to the 'Stans increased by €46bn in 2023, up 50% from 2021. That was equivalent to three-quarters of the drop in Europe's exports to Russia from 2021 to2023.

Last year, agricultural products flowing from Europe into Kazakhstan doubled from 2021 to 2023, official numbers show. Machinery exports to Kazakhstan from the EU doubled from 2021 to 2022, and then rose another 23% in 2023 to reach €6.4bn. Kazakhstan's tech industry of only 50 companies has seen exports to Russia rise from $40m in 2021 to $298m in 2023. Electronic imports from Europe also increased from €250m to €709m in the same period, *The Economist* reports.

Exports of goods like high-end washing machines from Europe to Kyrgyzstan and on to Russia have ballooned, some of which the Russians have been stripping for their sophisticated operating microchips that have then found their way into Russian missiles. Likewise, in Armenia's case trade has tripled, in Uzbekistan it leapt by 52% year on year and in Kazakhstan by 30% y/y.

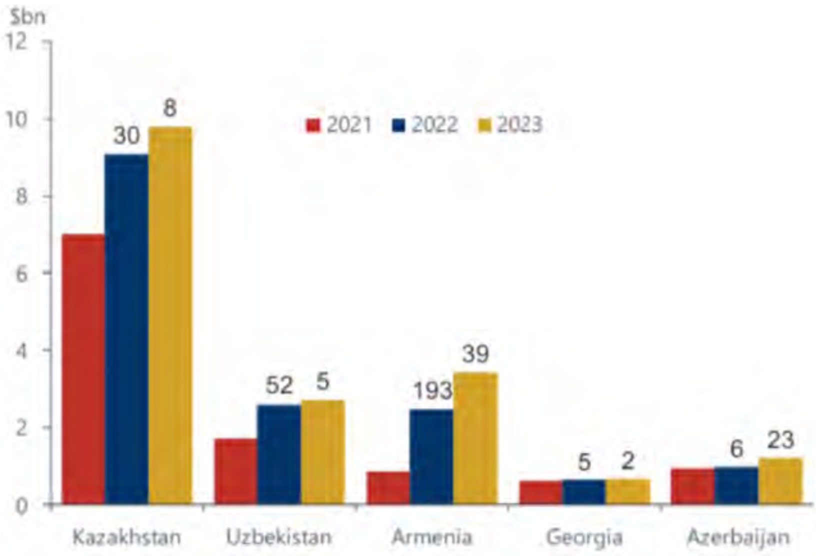
Armenia now imports twice the chemicals, five times the IT hardware and four times the electronics from Europe in 2023 as it did in 2021. Azerbaijan has also jumped on the bandwagon, by boosting sales of gas to Europe, despite the fact that it barely has enough to meet its own domestic demand; there has been speculation that it is exporting more of its own gas to the EU, but importing more Russian gas through the backdoor to meet the domestic shortfall, something the president denies.

Tiny Kyrgyzstan has probably been the biggest winner and Uzbekistan the least. Bishkek has seen trade volumes leap by thousands of per cent, fuelling an economic boom. Budget revenues have doubled and GDP growth in 2023 was over 8%. The only European country that has seen trade volumes with Central Asia fall is Poland, which has been making a genuine effort to enforce sanctions. Western Europe's companies seem happy to turn a blind eye to the fact that the demand for high-end Mercedes saloons or sophisticated computers suddenly spiked in what used to be the dirt-poor part of the Former Soviet Union (FSU).

And there is no sign that this trade is slowing down. Quite obviously, these countries are acting as transit routes to Russia for goods under sanction, but not only. As *bne IntelliNews* reported, the technology sanctions have largely failed and Russia has been able to source 98% of the machines and chips it needs from abroad in 2023, according to a report by the Kyiv School of Economics.

However, the majority of the trade is simply Central Asian countries stepping in to provide Russia with non-sanctioned goods that are no longer being sold to Russia by the EU. A study by *Bloomberg* found that only 7% of the goods being sent to Russia from Kazakhstan were sanctioned goods. This remake of supply channels has also spurred a boom in local investment to set up new production in what appears to be a permanent change in supplier relations, and it is working to Central Asia's advantage.

Most EMs in the CCA boosted goods exports to Russia in 2023-2024



Source: Oxford Economics/Haver Analytic; Data labels denote an annual percentage change

An EBRD report looked at the example of Kyrgyzstan, "whose textile sector expanded by 42% in 2022, with textile exports accounting for 45% of total exports to Russia... and will expand above potential in 2024 at 3.6%." All of the Caucasus countries – Armenia, Georgia and Azerbaijan – have seen similar steep rises in Russia import volumes since 2022.

The country that has benefited the least is Uzbekistan, which saw import growth of a relatively modest 13% in 2022 and 6% in 2023. Uzbekistan is double-landlocked, making it the most difficult and expensive of the 'Stans for the transit of goods from Europe to Russia.

A secondary side-effect from the war is that the influx of hundreds of thousands of Russian emigrants has also boosted local demand, pulling in more imports. Most have arrived with significant savings and have deposited millions of dollars in Georgian and Uzbek banks.

These factors have also pulled in growing imports from China as the 'Stans tool up to meet the burgeoning demand. Exports to Armenia, Georgia and Uzbekistan grew by double-digit rates in 2022-23.

"Over the last two years, the region has seen a sizeable increase in publicly and privately financed investment in transport, logistics and export-oriented manufacturing capacities. Robust growth in wages and real incomes, coupled with a surge in international arrivals and tourism, fuelled a consumption boom, further supported by technological advances in consumer lending," the EBRD said in the report.

Intra-regional trade, investment and tourism continued to rise, assisted by much-improved regional cooperation on common challenges ranging from water and energy shortages to transport and border management bottlenecks. Inflation receded to single-digit levels in all countries in line with broader global trends, allowing central banks in most Central Asian countries to reprioritise growth and start softening their monetary policy stances, according to the EBRD.

Kyrgyzstan renaissance

Previously dependant on agriculture and gold mining, the Kyrgyz Republic has taken its war windfall and poured it into multiple hydropower projects, led by the flagship Kambarata-1 hydropower power plant (HPP) that will increase the country's installed power capacity by half, provide the energy to boost the economic boom the small Central Asian country is already enjoying, and earn money for Kyrgyzstan through power exports to the rest of the energy-hungry region.

Economic growth is now running at 7-8% a year and the government's tax revenue doubled in 2023 on a combination of reforms and mushrooming trade, Kyrgyzstan's Chairman of the Cabinet of Ministers Akylbek Japarov told *bne IntelliNews* in June.

"Average GDP amounted to 7% and accelerated to 8.8% in the first quarter of 2024," he noted, reeling off an impressive array of macroeconomic results, including a doubling of tax revenues in the last year.

However, the nominal GDP of the country is still only $14bn, making Kyrgyzstan one of the poorest countries in Central Asia, with the region having a collective GDP of around $450bn. Nevertheless, all the macroeconomic indicators are rapidly improving, particularly inflation, which has fallen from double digits, caused by the effects of the recent polycrisis, to 4% this year.

However, the boom may have reached a peak. As reported by *bne IntelliNews*, the Russian economy probably reached peak at the end of the first half of this year and is now starting to cool as the military Keynesian factors that boosted economic growth are now exhausted. ●

Uzbekistan's textile sector booming, ready for the next phase

Ben Aris In Samarkand

Uzbekistan's textile sector is booming. Cotton has long been Uzbekistan's "white gold." Its importance to the country is so great that the cotton plant features in its national emblem; exports of its high-grade cotton sustained the country during the worst of the economy crisis that followed the collapse of the Soviet Union in 1991.

But in 2017 newly elected President Shavkat Mirziyoyev took the radical step of banning exports of raw cotton entirely. Industry was forced to go up the value chain overnight and massively expand the production of textiles. Private cotton farms were then set up starting in 2018 in what in effect was a large-scale privatisation of the entire cotton sector.

It was bold gamble and, as *bne IntelliNews* reported, it has paid off handsomely. Production is up five-fold since the textile modernisation campaign was launched at the start of the Mirziyoyev era and exports are up four-fold, of which only 10% comprise raw cotton and the rest are finished goods.

At the same time, the sector was privatised, broken up into just under 150 "clusters" where private investors were given long-term leases on land to grow raw cotton and were expected to set up complete vertically integrated production chains called clusters that run from growing cotton through to producing finished apparel and other products.

Today Uzbekistan exports to more than 80 counties, earning $3.4bn in 2023 from textiles based on the production of 1.3mn tonnes per year (typ) of raw cotton. More than $3.2bn has been invested in the sector, almost entirely by private companies, and the investment is ongoing as the sector continues to expand.

Uzbekistan's textiles sector is growing by leaps and bounds, but now it is well established its privately owned companies are looking to increase production again and cast their nets wider. / Ben Aris

"Uzbekistan has moved very fast in the last five years. A total of 142 clusters have been set up that are responsible for 100% of the country's textile production," says Karim Shafei, a textile expert based in Switzerland who was speaking to the delegates of the International Textile Manufacturers Federation (ITMF) Annual Conference and fashion convention in Uzbekistan on September 9. The ITMF is an international trade federation for the world's textile industries. "In the last eight years textile exports are up 200% from less than $3bn [in] 2022 to almost $4bn for this year. Within that, apparel exports have grown from $300m in 2017 to $1.4bn 2023 – a huge gain – and finished product exports are up five-fold."

Kamalak Cluster

Just outside the legendary city of Samarkand is the Kamalak Cluster. The total of 16,000 hectares of cotton fields, stretching away from the administrative buildings, are almost ready to harvest. The yellow flowers of the small shrubs have given way to fat green pods full of cotton that will burst in the coming weeks ready for the mix of advanced John Deer harvesters and a workforce of 1,500 professional cotton-pickers to move into the fields.

From there the raw cotton is transported to factories less than an hour's drive away to be processed into thread before finally being worked into textiles and turned into finished products by companies that belong to the group.

The cluster already generates some $20mn worth of finished products every year that are exported to over 58 countries, according to Tadjiev Mukhiddinovich, the chairman of the cotton-textile cluster association, who travelled to Kamalak to show-case the farm.

The company is owned by Zafar Hakberdiev, a local entrepreneur, who invested $30mn into the business, partly from his own funds and partly using a credit from Germany's LBBW Bank. One of the weaknesses of the Uzbekistan economy is that borrowing rates in soum, the local currency, are still prohibitively high, leading companies to prefer the much cheaper credits denominated in foreign currencies; however, these expose the economy to an FX risk, should a shock cause a deep devaluation.

Like all the clusters, it is privately owned and the investment capital comes from investors who are free to funds the project, as they are able. The distribution of over a hundred lots means no one company dominates the business, although there are no formal restrictions on how many clusters a company can own, which suggests eventually the sector will consolidate into a few large players. The only aid the government offers is through long 25-year leases on the land and some so-called loose loans to buy machinery.

In addition to its own business, Kamalak has a joint venture with the Singaporean multinational company Indorama, which is investing into the development of the textile sector around the world. It also cooperates with the US financiers Silverleafe and the Turkish Maroqand Development Cluster. Germany's Federal Ministry for Economic Cooperation and Development (BMZ) is acting via the German Cooperation Agency for International Development (GIZ), a German state-owned company, and implements the majority of BMZ's technical development cooperation, which is active in Uzbekistan.

"After the 2016 reforms, foreign investors are treated like locals and given the same opportunities," says Mukhiddinovich. "The foreign investors are allowed to open a cluster and the right to rent the land for up to 25 years, which remains owned by the state."

Mukhiddinovich says the reforms have been very successful. Previously the sector was divided into farmers and textile producers, but now it has been united in the cluster system and under private management, the output of the farms has soared.

Closer to town on the outskirts of Samarkand is the textile factory where the raw cotton is transformed into thread and even closer to the city is the Samarkand Carpets (SAG) rug and clothes showroom, and shirt factory. On the first two floors of the modern business is a swanky showroom for the company's carpets, for which Uzbekistan is famous, and these are a must-have household item in Uzbek culture. Families and couples are strolling in

the air-conditioned showroom, looking over a wide selection of the large carpets that are made with the cotton from the Kamalak farm. The walls are lined with a wide selection of shirts, some under the company's own SET brand and other using the designs of famous international designers.

Upstairs on the third floor is a small factory with lines of women working at sewing machines producing the shirts on sale downstairs.

"Most of the workers are women, but things have changed, as they work in shifts and usually do few days on and then take a few days off," says Shukhrat Makhsudov, SAG's director, who oversees the production and sales. The factory is brightly lit with windows all around the floor and a large ventilator blasts out cool air, creating a pleasant breeze on the shop floor where the women work at their machines.

Samarkand SEZ

The ancient Silk Road way station of Samarkand is once again buzzing with foreign visitors. An Uzbek innovation hub, there are more than 600 international companies present and 60 fast growing production facilities that have doubled their output in the last five years, according to the region's governor, Erkinjon Turdimov.

The state has established a Special Economic Zone (SEZ) that offers tax breaks and other benefits to attract investors. The local entrepreneurs say wryly that the investors have it better than them, as there is a special foreign investment law that gives foreign investors even more rights than they enjoy – the government has been full focused on attracting foreign investment to accelerate the country's development, but only if they can bring added value.

Uzbekistan has one of the fastest growing populations in the world, adding more than 1mn people a year, and 100,000 per year in Samarkand alone. With a regional population of 4.2mn people, Samarkand is one of more populous regions in the country, the local governor says.

Shafei points out that although the EU markets are only a few days away, one the problems that Uzbekistan still faces is that it remains largely under the radar for most Europeans and Americans firms, and for those that know the country, the legacy of the previous ban on Uzbek cotton means they are reluctant to do business.

Starting in Soviet times and extending into the regime of former president Ismail Karimov, the first present of independent Uzbekistan who died in 2016, the government routinely pressed students and children into service to bring in the cotton harvest. This led to an international boycott of Uzbek textiles. After taking office, one of the first things Mirziyoyev did was end the practice and the ban was eventually lifted in 2019, but it has sullied Uzbekistan's reputation.

> "Uzbekistan has moved very fast in the last five years. A total of 142 clusters have been set up that are responsible for 100% of the country's textile production"

The fact that the ITMA chose to hold its global annual general meeting in Uzbekistan is a testimony that the Republic has been forgiven for its past transgressions and has been welcomed back into the fold of respectable textile manufacturers as delegates from around the world travelled to Samarkand for the meeting that was not exclusively focused on the rapid growth of Uzbek textiles.

"Uzbek textiles needs to work on its image and showcase the changes. It needs to create a new image as a dynamic, low cost, high quality producer of textiles," Shafei said. "Uzbekistan [is] not known to EU [or] US buyers or [has] a negative image, so there is a lot of work to inform the world and change the reputation."

The already vibrant textile sector still has more work to do if the country is to fulfil its ambition of becoming a global textile production powerhouse. The first multinationals are starting to arrive, with small deals with Nike and Adidas in 2020, but the really big household fashion and apparel names have yet to move in and source large volumes from Uzbekistan.

Key to the initiative has been reaching out to new partners. The government is now building four industrial zones that are totally dedicated to textiles and include infrastructure such as renewable energy, water treatment plants and other sustainable development elements that have become essential for the industry. A speaker from the EU at the ITMF event gave a presentation explaining that the EU will implement new sustainable production regulations for textiles in 2025 that will lift the barrier to entry a little higher for the EU's import partners and force them to implement higher ESG standards.

The US and EU have already become key export destinations, especially after Uzbekistan signed a key GSP+ preferential trade deal in 2021, and it also has free trade agreements with all of the other members of the Commonwealth of Independent States (CIS) countries. But it is seeking to expand its reach further both in terms of market and investment partners.

"German, Korean, Singaporean companies and many other have invested and playing in our market," says Samarkand Governor Turdimov. "But we are hoping to attract more investment from other countries."

Part of the government's decision to step beyond the cotton sector entirely has been motivated by its efforts to join the WTO; the trade club's rules preclude countries that subsidise sectors such as textiles.

Another goal is to provide jobs for the burgeoning population. With an average of age of only 28, Uzbekistan needs to generate decent jobs for its young population.

"The goal is not simply to provide new job opportunities but decent job opportunities," Turdimov told the summit's delegates in Samarkand.

The local brands also need to be developed and here Uzbekistan's Silk Road history can be a big advantage, as cities like Samarkand are already the stuff of legend and its fame has already driven the explosive growth in tourism in recent years.

In the next phase Uzbekistan needs to diversify its markets and embrace new materials. "Uzbekistan has regional market but there is a ceiling. We have to look at non-traditional markets like North Africa, further afield in Europe and Asia," Shafei told the delegates at the ITMF event.

"There has been lots of investment into machines with huge factories and state-of-the-art equipment, but Uzbekistan is double-landlocked and logistics remain difficult to manage with the current geopolitical situation. The government has provided support to logistics but it remains a challenge and it is still not fully utilising the closeness to Europe," Shafei said.

Uzbekistan would love to export textiles to Southeast Asia as well, but currently its southern route into Asia is blocked by the instability in Afghanistan. Delegates from Asia to the ITMF annual summit told *bne IntelliNews* that currently there are no direct textile exports to Pakistan or India, but some Uzbek textiles goods are traveling there via intermediaries like Indonesia.

Delegates at the event also said that in the next phase Uzbekistan needs to embrace man-made fibres as part of its textile sector. Some polyester is starting to be used, but as *bne IntelliNews* reported, Uzbekistan's plastics industry is still in its infancy. But that will change when the very large MTO petrochemical complex in Bukhara comes online in about four years' time to produce the raw materials to create a variety of man-made fibres for the country. ●

Nino Dolidze, of Georgia's International Society for Fair Elections and Democracy

Ailis Halligan in Tbilisi

Georgia's leading election watchdog rejects the ruling party's foreign agents law and will "defend the will and rights of Georgian voters" in next month's elections, says Nino Dolidze, the executive director of the Tbilisi-based International Society for Fair Elections and Democracy (ISFED).

"ISFED was created to support Georgia's free and fair elections. Any money we've received from foreign donors has been for the development of Georgia's democracy. We are not representing any other country's interests. We will never call ourselves 'agents' – it's against our dignity", Dolidze told *bne IntelliNews* in an interview in the Georgian capital this week.

In the run up to crucial elections which will determine Georgia's future global allegiance, such an act of public disobedience could jeopardise ISFED's role as election observer. However, Dolidze is determined the society will continue its work safeguarding the democratic process and advocating for real democracy in Georgia, and will resist pressure from the governing Georgian Dream party, which critics say is shifting Georgia away from the West and towards Russia.

"We don't tell voters which party to support, we just want to make sure that they are voting in free and fair elections. We think the watchdog role and challenging non-democratic steps are important," Dolidze says.

ISFED is joining the majority of Georgia's non-governmental and media organisations in a boycott of the "law on the transparency of foreign influence", passed in May this year. Both critics abroad and the Georgian political opposition have spoken out against the legislation – dubbed the 'Russian law' – which they say aims to stigmatise organisations, stifle voices critical of the government and stir up anti-Western propaganda.

The controversial law requires all Georgian NGOs that receive at least 20% of their funding from abroad to publish voluminous details of their assets in an online portal by September 2nd, a deadline which has now passed. Organisations that failed to comply are now subject to fines of GEL25,000 ($9,200) and will be forcibly registered by the government.

The "transparency of foreign influence" law has been compared to similar legislation passed in Russia in 2012, which has been used since to systematically eradicate all free and independent media.

Dolidze says the Georgian law serves to discredit, stigmatise and whip up distrust of those organisations that are internationally funded, albeit that that money is spent doing work inside Georgia, and, in the case of ISFED, preserving democracy and protecting voters' voices.

Red Herring

Georgian Dream insists that a law on transparency is essential against a backdrop of alleged heavy interference by foreign powers in Georgian politics. Tbilisi Mayor and party secretary general Kakha Kalazde recently commented on many NGOs' "transformation into political entities funded from abroad", signalling the ruling party's wider suspicion of a so-called 'Global War Party' which backs Georgia's radical pro-Western opposition and wants to involve Georgia in the Ukraine war, a fantasy promoted by the party's founder, Bidzina Ivanishvili, who made his fortune in Russia.

Dolidze, like Georgia's pro-Western opposition, argues that concern over honesty and openness surrounding NGOs funding is a convenient red herring Georgian Dream is using to distract from the foreign agent law's true intentions.

"The organisations being targeted have details of their finances on their website. We [ISFED] have always been transparent about our money", she says.

The law's true aim, Dolidze says, is to pose an existential threat to NGOs, as the fines the government can issue to those organisations unwilling to register as foreign agents are so high that "you can't really pay and exist at the same time". "We don't know how far the government might go", the ISFED director adds.

As part of their public rejection of the law, ISFED refuses to register themselves with the government's online database of organisations that suggests they are "serving the interests of a foreign power".

Such invasive legislation not only represents a violation of privacy and basic human rights but also a breach of Article 78 of Georgia's constitution, Dolidze explains. This states that all the country's state institutions should follow a pro-Western trajectory, yet Brussels has warned that the current authoritarian course of the government blocks Georgia's path to EU membership.

With its operations almost entirely funded from overseas, primarily by democracy-supporting foundations such as USAID, NED and SIDA, ISFED is one among nearly 30,000 independent media and civil society organisations in Georgia that have been targeted by the foreign agent law.

"The government have always targeted civil society organisations, especially ISFED, and now they've created this law as an instrument to silence free voices in Georgia. This is just one component to discredit and attack civil society organisations. We will not let it happen. We will fight for freedom of speech and freedom of expression," Dolidze says.

As one of Georgia's oldest and largest civil societies, ISFED finds itself repeatedly in the ruling party's line of fire. But such a reputation has pushed them to "take the lead", Dolidze says, both in renouncing the foreign agent law and in fighting the legal battle against it. Whilst they may be front runners, she continued, the courage and integrity of smaller organisations should not be underestimated. "We are all together in this fight at the same level", Dolidze says.

'Traitor to the nation'

121 organisations have joined ISFED, Georgian President Zourabichvili, and members of the parliamentary opposition in appealing to Georgia's Constitutional Court to challenge the law on the 'transparency of foreign influence'. Dolidze explained they are now awaiting a decision, which they hope will be reached autonomously, although it could very well be politically influenced, as is not uncommon in Georgia.

"If they [the Constitutional Court] want to make an independent decision then they have more than enough evidence, first, to mitigate the immediate effects of the law as an interim measure, and then, following discussion, to abolish it entirely".

Disobeying the ruling party comes with personal risks. During the demonstrations of April and May before the law was passed, Dolidze says she and other protesters were verbally attacked and harassed in text messages. She was not physically harmed, while others were, but Georgian Dream representatives defaced her front door with graffiti declaring her a "traitor to the nation".

"We do not exclude anything now because we have seen the face of this government during rallies", Dolidze said.

Indeed, with the election stakes so high, the pre-voting environment is set to grow ever more febrile in the coming weeks, with the ruling party working to "control the free will of voters, especially in the regions and especially among public sector workers who are scared to lose their jobs", explains the ISFED director.

With full control over state institutions and a monopoly on administrative resources, the ruling party is implementing "big social and infrastructural programmes to steal the hearts of voters", while other parties don't get the same opportunities, Dolidze says.

ISFED's goals in the run up to and during the elections aim to counter this far from balanced political environment. "Firstly, each and every vote matters", says Dolidze, explaining that voter education and high voter turnout is the most effective way to combat election manipulation, which may occur from any side.

Of equal importance is protection of the votes themselves, but not necessarily defence of voters' choices. "To be professional we have to observe these elections objectively", she says, "we will flag any manipulation or violation from both the ruling party and the opposition, no matter what". ●

Nino Dolidze,
the executive director of the Society for Fair Elections and Democracy. IFSED

Armenia has split with Russia politically, but the realities on the ground mean that Russia continues to be a major trade partner. / bne IntelliNews

COMMENT

How Armenia helps Russia bypass Western sanctions

Seymur Mammadov in Baku

Armenia must adhere to a multi-vector foreign policy while effectively managing risks, as Prime Minister Nikol Pashinyan stated two years ago during a lecture in the Netherlands. But that includes the necessity of trading with Russia despite the extreme sanctions imposed only days after the war in Ukraine started two years ago, for the sake of keeping the economy afloat.

In April this year, Yerevan again stated the need for diversification, stressing that this strategy has become not just theoretical but a reality for the country. Pashinyan has repeatedly claimed that Armenia follows a consistent multi-vector foreign economic policy. However, upon deeper analysis, it becomes clear that the proclaimed multi-vector approach does not reflect the actual situation. Yerevan's real policy resembles a forced choice between the interests of major players rather than a fully balanced multi-vector strategy implying equal relations with various partners.

Today, Armenia is slowly but steadily moving toward the West while simultaneously benefiting significantly from trade with Russia. Despite Yerevan's official statements, relations with Moscow are not as strained as they may appear at first glance. This is evident from Armenia's economic indicators, which are growing due to the re-export of Russian products that have come under sanctions.

Since the start of the Russia-Ukraine war in 2022, Armenia, the country with the smallest foreign trade volume in the South Caucasus, has faced a sharp increase in both imports and exports, a surge that seems disproportionate to its economic potential. The expansion of sanctions imposed by the European Union and the US against Russia has led to reports indicating a significant rise in trade between Armenia and Russia.

Changes in the structure of goods flows and trade destinations between 2021 and 2023 are largely linked to circumventing Western sanctions against Russia. In 2021, Armenia's foreign trade turnover with Russia increased by 24.2% compared to 2020, reaching $2.6bn. In 2022, it skyrocketed by 93.4%, amounting to $5bn, and in 2023, the growth continued at 45.7%, with turnover reaching $7.3bn. According to Alexey Overchuk, the First Deputy Chairman of the Russian Government, at an intergovernmental commission meeting on economic cooperation with Armenia, trade turnover between the two countries could reach $14-16bn in 2024. Should this forecast materialise, Armenia's foreign trade volume with Russia would increase eightfold compared to 2020.

According to Armenia's National Statistical Committee, exports to Russia in 2022 tripled compared to the previous year, reaching $2.4bn. In 2023, this figure rose by 43.1%, hitting a historical high of $3.4bn. Between 2010 and 2020, the average annual growth rate of Armenian exports to Russia was 18.6%, while from 2020 to 2023, this rate sharply increased to 64%.

Russia's share in Armenia's total exports, which stood at 27% in 2021, increased to 40-44% in 2022-2023. This growth can be attributed to Armenia's strategy of circumventing sanctions – the country imports goods from the European Union, the Gulf and Asia, followed by re-exporting them to Russia. In 2023, 14.7% ($499mn) of Armenia's exports to Russia consisted of telecommunications devices, 11.1% ($378mn) were passenger cars, 7.39% ($250mn) were monitors and projectors, 2.54% ($86mn) were calculators and their parts, and 1% ($31mn) were vacuum cleaners. In total, 91% of Armenia's electromechanical equipment exports are directed to Russia. Additionally, exports of nuclear reactors and mechanical devices to Russia increased tenfold, and exports of optical instruments and medical equipment grew fivefold. Exports of aircraft doubled, while exports of ships and boats increased eighteenfold, musical instruments thirty-eightfold, and works of art and collectibles 19-fold. Many of these products had never previously been exported to Russia.

Despite the EU's sanctions against Russia, some EU countries continue to trade with Russia through Armenia. Notably, Armenia's trade turnover with the EU increased 2.4 times in 2023 compared to 2021, especially with countries such as Greece and Cyprus, where Armenian exports surged 39 and 24 times, respectively. This raises questions about the consistency of EU and US policies on sanctions against Russia when the very countries imposing these restrictions engage in trade through Armenia, effectively providing Russia with a "trade lifeline", thereby indirectly supporting its actions in Ukraine.

At a press conference following the Antalya Diplomatic Forum on March 2, Russian Foreign Minister Sergey Lavrov stated that Yerevan had made a "deliberate decision" to pursue a course of deteriorating relations with Moscow. "We regret that the Armenian leadership has apparently made a conscious decision to consistently worsen relations with the Russian Federation, blaming Russia for everything that has happened with Nagorno-Karabakh. This is certainly not the behaviour of an ally. The Armenian leadership has decided to bet on extra-regional countries, which are courting Yerevan and promising to help with all its problems, as long as Armenia 'cuts ties' with Russia and the integration structures created in our shared region. It takes political courage to admit that since 1991, Armenia has followed a fundamentally wrong course in relations with Russia. If this is the assessment of the entire Armenian leadership, based on the opinion of the people, then much in the Russia-Armenia relationship needs to be reconsidered," Lavrov said.

Despite growing political tensions, economic cooperation between the two countries remains stable. While Lavrov's statements were harsh, economic ties between Russia and Armenia not only persist but also show significant growth. The worse the external relations between Moscow and Yerevan, the greater the trade turnover.

In early June, Germany's DW conducted an investigation and published its findings. It is known that, since January this year, in line with the 12th package of EU sanctions, a full ban on the direct import of non-industrial natural and synthetic diamonds and diamond jewellery from Russia to the EU came into effect. A partial European embargo on Russian diamonds processed in third countries was introduced on March 1, with the full ban taking effect on September 1. As DW reports, gold is exported from Armenia under the guise of Armenian origin, although the country has never produced this metal in such quantities. In 2023, according to official statistics, Armenia exported $1.8bn worth of gold and $589mn worth of diamonds. Since the beginning of 2024, Armenia has already exported $2.5bn worth of gold and nearly $200mn worth of diamonds. The processing of precious raw materials has increased by 31%.

"Armenia serves as a transit point not only for the re-export of Russian products but also for the re-export of European goods to Russia"

Armenia serves as a transit point not only for the re-export of Russian products but also for the re-export of European goods to Russia. According to Armenian media, since 2022, Armenia has been supplying the Russian Federation with mobile phones, household appliances, and vehicles of European, US and other origin. Armenia itself does not produce these goods.

Nikol Pashinyan's proclaimed "multi-vector" approach is not limited to the re-export of sanctioned Russian goods to other countries and the transshipment of European goods to Russia. Yerevan is also diversifying its arms purchases. After harsh statements from the Armenian side toward Moscow, the expulsion of Russian border guards from Zvartnots Airport, and Russia's acute need for weapons, it was expected that arms deals between the two countries would be halted once and for all.

However, it was recently revealed that Russia has resumed arms supplies to Armenia under previously concluded contracts. Specifically, this concerns the supply of rockets for the Smerch multiple-launch rocket system. A year ago, Russian media reported that the rocket manufacturer NPO Splav had approached Yerevan about the readiness of an order for shipment, but the Armenian side did not collect the rockets. It was also reported that after the 2020 war Russia offered and was ready to supply Armenia with weapons and ammunition on credit for amounts of $1bn and $400mn. The smaller contract was approved and ready for signing, and only days remained before the approval of the $1bn contract when Armenia abruptly rejected the agreements. Instead, Iran and Armenia have signed a major arms deal worth $500mn. Additionally, Armenia has become the largest buyer of Indian weapons. As reported by Report, citing data from the Indian agency IADN and the Ministry of Defence, the total amount of arms purchases by Armenia will reach $600mn in the 2024-2025 fiscal years. Since 2021, Armenia has been actively acquiring missiles, artillery systems, air defence systems and other weapons from India.

India, according to official data and various sources, is actively strengthening military-technical cooperation with Armenia. Between 2023 and 2024, Yerevan purchased a wide range of weapons from India, including advanced missile systems, air defence systems, tanks, armoured vehicles, howitzers, small arms, and unmanned aerial vehicles. These supplies significantly bolster Armenia's defence capabilities amid the unstable geopolitical situation in the region. In addition to cooperation with India, Armenia is also actively purchasing weapons from France, indicating an expansion in the geography of military supplies and a desire to diversify arms sources. Moreover, Azerbaijani media reported on the potential supply of American military equipment.

It is noteworthy that Armenia's arms purchases from Nato countries, including France and the US, have not become an obstacle to receiving Russian missiles, indicating the continued strong ties with Moscow in the military sphere. The question remains whether Armenia will return to previously suspended contracts with Russia given the changing political and economic situation." ●

Russia gets ready to rebuild its military stockpile

Ben Aris in Berlin

Russia is set to embark on a long-term military reconstitution programme aimed at restoring the losses incurred during its full-scale invasion of Ukraine. Russian President Vladimir Putin has already increased the upper limit of men under arms to 1.5mn on September 16, but the biggest challenge will be to equip them and replace the materiel already used over the last two years of war – and pay for it.

Europe is facing the same dilemma, but, as *bne IntelliNews* reported, has a much more serious shortfall and a lot less money to spend on rearming. Germany, in particular, will not be able to return to pre-war levels of armament for decades.

While the Kremlin has yet to finalise the future design of its armed forces, the broad outline of its strategy is beginning to take shape, according to analyst Dara Massicot in a recent in-depth report for the Carnegie Endowment for International Peace.

Massicot warns that reconstituting Russia's military should not be viewed as a simple restoration of pre-war personnel and equipment numbers. "Reconstitution is a process of regaining combat functions, proficiency and capabilities that will allow a force to execute various types of combat missions," she explains. How the army will be rebuilt will depend on what Russian President Vladimir Putin wants to do: conquer the Baltic States, or defeat Nato in a world war.

Since its invasion of Ukraine, Russia has focused on reconstituting its forces without placing its economy on a full wartime footing. This has involved partial mobilisation in 2022, repairing existing equipment, purchasing weapons and ammunition from abroad to supply ongoing operations and offering substantial financial incentives to attract volunteer soldiers in lieu of a general call-up. However, Russia's military production capacity, apart from the notable exception of drones, has plateaued as of early 2024. "Russia could generate more efficiency by reducing corruption on the margins and emphasising innovation, but this would not result in a dramatic increase in available resources," Massicot notes. To make a serious attempt to bring stockpiles back to pre-war levels will require a complete retooling of the entire Russian economy.

Economic strain and mobilisation

To significantly increase weapons production or manpower, Russia would need to activate further mobilisation powers, which would have profound effects on the economy, labour market, and public engagement with the war. "The Kremlin's

Visually Confirmed Russian Equipment Losses, February 2022-April 2024

Equipment Type	Losses as of April 8, 2024	Prewar Number in Active Duty (Reserves)	Percentage of Total Losses, Active Duty (Active Duty Plus Reserves)
Main battle tanks	2,500–2,900	2,840 (10,200)	>100 percent active prewar (18–21 percent)
Armored personnel carriers and infantry fighting vehicles	4,800–5,400	14,280 (15,500)	34–35 percent active prewar (16–17 percent)
Self-propelled artillery and multiple rocket launchers	980–1,080	3,024 (7,480)	32–36 percent active prewar (9–10 percent)
Air defense systems	220–290	2,234	10–13 percent
Helicopters	94–135	821	11–16 percent
Fixed-wing tactical aircraft	71–99	1,172	6–8 percent
Ships (Black Sea Fleet)	13	58	22 percent

Sources: Jakub Janovsky, naalsio26, Aloha, Dan, Kemal and Alexander Black, "Attack On Europe: Documenting Russian Equipment Losses During The Russian Invasion Of Ukraine ," Oryx, February 24, 2022.

calculus and political will have so far constrained Russia from taking such a step," says Massicot.

And all the new equipment needs to be paid for. Currently, direct Russia spending on the military is about 8% of GDP on defence or around $100bn a year. Military spending at the current level is likely to be sustainable to 2026.

The Federal Budget Law for 2024-2026 passed last year envisages another year of fiscal expansion in 2024, rising from total expenditure of RUB30.5 trillion ($330bn) in 2023 to RUB36.7 trillion in 2024. This increase in spending is driven by a planned hike in the "national defence" portion of the budget, which is scheduled to rise from RUB6.4 trillion ($70bn) to RUB10.8 trillion.

Other areas of the budget, such as the "domestic security and law and order" portion, are also used to finance military expenditure. Total defence spending is likely to exceed RUB13 trillion ($155bn). Social spending will rise by close to 20% in nominal terms from RUB6.5bn this year to RUB7.7bn; however, it will remain far below military expenditure. Other categories of spending are only expected to increase slightly, with most expected to rise in line with inflation.

Russian leaders continue to justify their reconstitution efforts by framing the need to replenish forces as a response to Nato expansion rather than admitting the high costs of the war in Ukraine. For now, the country is relying on refurbishing older equipment and recruiting personnel, but many of the weapons deployed are qualitatively inferior to newer models, and stockpiles of Soviet-era equipment could be depleted by 2026 if loss rates continue at current levels.

The medium-term challenge for Russia, according to Massicot, is whether it chooses to expand its forces rapidly or manage a more gradual build-up, balancing military needs with domestic stability.

"If expanding the force is of paramount importance, the current reconstitution efforts will be insufficient. Leaders will likely be forced to take steps they have so far resisted, such as activating more mobilisation powers and expanding domestic production capacity," she writes.

"If, however, Russia prioritises economic stability, it could accept the risk of relying on existing production levels and older Soviet equipment. This strategy would be feasible only if the conflict in Ukraine freezes or ends, allowing time for a gradual build-up of new equipment through the 2030s," Massicot adds.

Capacity limitations

Russia's ability to increase new military equipment production is currently hampered by several structural factors.

"Space at Russian defence factories is in high demand for multiple purposes – new builds, repairs and exports – and cannot be easily converted to increase domestic production without trade-offs," explains Massicot. Expanding production would require new factories or halting exports, both unlikely moves in the short term.

Additional options include converting civilian factories into wartime production facilities or importing military equipment, though such measures would signal a significant departure from historical norms.

"Russia could opt to import armoured equipment from other countries, but this would suggest an unwillingness to accept short-term risks and an intention to continue offensive actions against Ukraine," she adds.

Challenges in personnel reconstitution

Rebuilding Russia's military personnel base will also prove difficult. Wartime retention policies have prevented servicemen from resigning, masking the broader impact of the war on recruitment. While the government is offering higher wages and social benefits to attract recruits, maintaining these levels of expenditure in the post-war years would strain an already bloated defence budget.

Vladimir Putin has increased the authorised strength of the Armed Forces for the third time since the start of the war – to 2.389mn people, of which 1.5mn are military personnel – by decree on September 16. In just two years, the Russian army has already grown by one and a half times. This increase will cost the budget, the drafting of which is in full swing, very dearly.

Increases in expenditure are difficult to support without a corresponding rise in revenues. However, Moscow has performed exceptionally well in this respect. Federal budget revenues are projected to rise from RUB28.7tn last year to RUB35.1 trillion in 2024, bringing down the budget deficit to 0.9% of GDP.

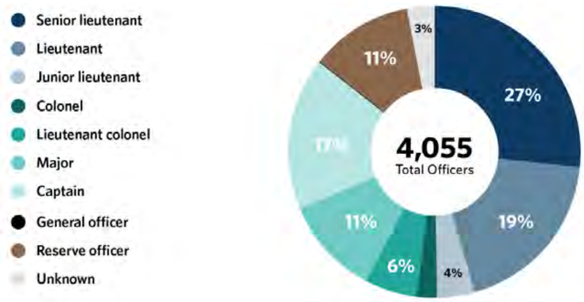
However, the Russian economy is already cooling and expected to slow sharply in 2025. That means a shift toward a full mobilisation scenario would place the budget under much greater strain. The Kremlin would be forced to increase taxation to finance the significant expansion of military spending entailed under this scenario, pushing total federal revenues to closer to 25% of GDP. Raising these taxes would draw financial resources away from households and enterprises, suppressing the potential for growth in consumption and investment, which in turn would probably slow the rate of growth. Spending on other areas of the federal budget would also be squeezed.

"At the current level of spending, and with the existing productive capacity of the defence-industrial base, reaching the targets assumed in the partial mobilisation scenario would prove difficult, especially in those areas where Russia's wartime losses are highest. Russia's military would be large, but the standard of equipment would vary dramatically across units," says Massicot.

Expanding the force will require significant investment in new equipment and infrastructure, as well as recruiting professional soldiers in a society where high wages and social entitlements are expected. "These expenses would coincide with procurement pressures on an already strained budget and male labour force," Massicot notes.

Despite large untapped human resources, such as reserve officers and women in the military, Russia has so far chosen stopgap measures like shortening military training and recruiting from prisons or abroad. Expanding the roles of women or drawing deeper into reserve forces could indicate plans for a larger military force in the future.

Russian Officers Killed in Action by Rank, Feb 2022-Apr 2024



Source: "KIU Russian Officers Killed in Ukraine — Public Full Data Sheet."

A return to a mixed readiness system?

Massicot suggests that Russia may ultimately return to a "mixed readiness" system, combining a smaller active-duty force of around 1mn with a large combat-experienced reserve. This system, reminiscent of the late-Soviet era, would allow Russia to maintain military potential without the costs associated with a larger standing army. "Such a force would resemble the return of the mixed readiness system of the late-Soviet and immediate post-Soviet era, a significant departure from the last twenty years of force posture," she writes.

Russia's ability to capture and implement lessons from its military experience in Ukraine will be crucial to shaping its future force structure. "Formal learning organisations will likely be set up in the post-war years to analyse and disseminate findings, influencing operational concepts and force design," Massicot concludes, though political sensitivities and censorship could impede this process.

As Russia navigates the balance between rebuilding its military and managing economic constraints, the outcome of its reconstitution efforts will shape the country's defence posture for years to come. ●

Dara Massicot is a senior fellow in the Russia and Eurasia Programme at the Carnegie Endowment for International Peace. Her work focuses on defence and security issues in Russia and Eurasia. Prior to joining Carnegie, Massicot was a senior policy researcher at the RAND Corporation and senior analyst for Russian military capabilities at the Department of Defence. She has published extensively on Russian military capabilities, modernisation efforts and strategy, and is a pre-eminent expert on the Russo-Ukrainian War.

TEHRAN BLOG

Turkey, Iran and India vie for influence in Central Asia

This modern iteration of the 'Great Game' is playing out against a backdrop of shifting geopolitical priorities. / bne IntelliNews

bne Tehran bureau

As the world's attention pivots towards flashpoints in Europe and the Pacific, a new contest for influence is quietly unfolding in the heart of Eurasia. Turkey, Iran and India are stepping into the vacuum left by distracted global powers, each bringing its own strengths and strategies to the table in a bid to shape the future of Central Asia.

This modern iteration of the 'Great Game' is playing out against a backdrop of shifting geopolitical priorities. Russia, long the dominant force in the region, finds its attention and resources increasingly consumed by the conflict in Ukraine. The United States, having withdrawn from Afghanistan, is preoccupied with challenges in the Indo-Pacific. China, while still a significant player through its Belt and Road Initiative, is grappling with internal economic pressures and tensions over Taiwan.

Into this arena step three ambitious so-called middle powers, each with its own vision for Central Asia's future.

Turkey and Iran

Ankara's strategy revolves around the development of the 'Middle Corridor', an ambitious transport route linking China to Europe via Central Asia, the Caucasus and Turkey. This vision aligns neatly with Turkey's longstanding desire to leverage its geographic position as a bridge between East and West.

Turkish President Recep Tayyip Erdogan has been particularly active in promoting this initiative, seeing it as a way to boost Turkey's economic and political clout. The country has invested heavily in infrastructure projects across Central Asia, from railways to logistics hubs, aiming to position itself as the indispensable link in this new Silk Road. However, Turkey's ambitions face a significant hurdle: geography. To fully realise its Middle Corridor dream, Ankara needs to secure a route through Armenia: the proposed 'Zangezur Corridor'. This remains a contentious issue, not least because it has raised alarm bells in Tehran.

Iran, for its part, views itself as Central Asia's natural partner. With a shared cultural and historical heritage, and crucially, a direct land border with Turkmenistan, Iran offers Central Asian states their most direct route to international waters.

Tehran's approach has been multifaceted. On the economic front, it has been promoting its southern ports, particularly Chabahar, as the ideal export route for landlocked Central Asian countries. The recent visit of Turkmenistan's leader to Tehran, resulting in four strategic cooperation documents, underscores Iran's diplomatic push in the region. But Iran's strategy goes beyond economics. In a region wary of security threats, Tehran has been positioning itself as a reliable partner in counterterrorism efforts. The inauguration of a drone production line in Tajikistan last year was a clear signal of Iran's willingness to engage in military cooperation with Central Asian states. Moreover, Iran sees engagement with Central Asia as a way to mitigate the impact of Western sanctions. By fostering closer ties with its northern neighbours, Tehran hopes to create new economic lifelines and reduce its international isolation.

India: the democratic alternative

India, the latest entrant in this contest, brings its own unique proposition to Central Asia. As the world's largest democracy and a rapidly growing economy, New Delhi presents itself as an alternative to both Russian paternalism and Chinese economic dominance. India's primary focus has been on enhancing connectivity. The centrepiece of this strategy is the International North-South Transport Corridor (INSTC), a multi-mode network of ship, rail and road routes for moving freight between India, Iran, Afghanistan, Central Asia and Europe.

Central to this vision is the development of Iran's Chabahar Port, in which India has invested significantly. This project aims to bypass Pakistan, offering India a direct route to Afghanistan and Central Asia. Despite the challenges posed by the Taliban's return to power in Afghanistan, India remains committed to this initiative. Beyond infrastructure, India has been leveraging its soft power, offering scholarships to Central Asian students and promoting cultural exchanges.

It has also been quietly expanding its security cooperation, conducting joint military exercises and offering training programmes.

For Central Asian countries, this renewed attention from regional powers presents both opportunities and challenges. On one hand, it offers the prospect of increased investment, improved connectivity, and a chance to reduce dependence on Russia and China. On the other, it risks pulling these nations into new geopolitical competitions. Each of the contenders faces its own hurdles. Turkey's ambitions are constrained by geography and its complex relationships in the Caucasus. Iran's efforts are hampered by international sanctions and regional suspicions about its intentions. India, while offering an attractive partnership, struggles with limited resources and the logistical challenges of reaching Central Asia. Moreover, Russia and China remain significant players in the region. Moscow's security guarantees and China's economic heft cannot be easily displaced, regardless of their current preoccupations elsewhere.

Looking ahead

As this new chapter of the Great Game unfolds, several key questions emerge. Can Turkey overcome the geographical and political obstacles to realise its Middle Corridor vision? Will Iran's combination of cultural ties, geographic proximity, and military cooperation prove compelling to Central Asian leaders? Can India translate its soft power and democratic credentials into tangible influence? The answers to these questions will shape not just the future of Central Asia, but also the broader balance of power across Eurasia. As Turkey, Iran, and India jockey for position, Central Asian nations find themselves with more options – and more complex choices – than they have had in decades.

What is clear is that Central Asia, long considered a backwater in global affairs, is again becoming a focal point of international competition. The region's vast natural resources, strategic location, and untapped economic potential make it an increasingly important piece on the global chessboard.

For policymakers in Ankara, Tehran and New Delhi, success in Central Asia could be transformative, offering new trade routes, energy supplies, and strategic depth. For the Central Asian states themselves, skilful navigation of these competing interests could lead to a new era of prosperity and autonomy. ●

War in Ukraine – where is the Western leadership?

It has been more than two years, but despite the fact that the West dwarfs the Russian economy, it has been unable to aid Ukraine to a victory in the war. What's the problem? Where is the Western leadership? / bne IntelliNews

Timothy Ash, Senior Sovereign Strategist at BlueBay Asset Management in London

Over two and a half years now into Putin's full scale war on Ukraine and I think the West should be asking itself where it has gone wrong. Why has the West, with a combined GDP of $60 trillion, thirty times that of Russia, been unable to give Ukraine the support needs to bring it a speedy victory? And sure, some will argue that the fact that Russia has not beaten Ukraine is in itself a victory, but the reality is that Ukraine's continued survival against overwhelming odds owes more to the bravery of Ukrainians than the support it has received from the West.

At the core of the West's failings is a fundamental lack of leadership, both within Europe, but I think also and more importantly from the US, as the supposed leader of the free world. The US here talks of US exceptionalism – well the war in Ukraine was the ultimate test of the US place as the leader of the West.

There has been a continuous timidity in the Western approach when it comes Putin's war on Ukraine, an over-appreciation of the threats and demands of Russia, and I think an under-appreciation of the importance of ensuring Putin does not win this war.

One can see the failures very early on from the Biden administration, and particularly from its national security leadership in continuously failing to read Putin. From the outset the Biden administration saw China as the biggest global threat to the US and the international order, mistakenly seeing Russia as a declining second or third rate power. I think here they failed to understand that the Putin regime saw itself as at war with the West, as Lavrov et al put it, of a battle between ideologies, between "western liberal market democracy" and "sovereign democracy" – the latter of which is a fancy term for a "hands off autocrats" deal with the West.

Importantly though Putin recognised this as an existential battle for the survival of his regime, and it's prime defence was attack – to subvert the system of Western Liberal Market Democracy from within, by using Russian money as a corrupting influence to corrupt our systems from within – backing far right and far left parties in the West, promoting centrifugal forces within the West, and buying influence in politics, academic, sport, the media, business, et al. For Putin it was the West or him, which is very different I think from the threat to the West from China. Xi loves the global status quo, he is happy for the two systems to exist side by side, as he still sees globalisation and international trade as the means to eventually secure hegemony with the US. For China it is a symbiotic relationship – and he has/had no desire to kill of the system (the West) that China fed off. But Putin saw his survival in killing off Western Liberal Market Democracy. I don't think Biden, Blinken or Sullivan ever got this, and still don't. I dont think they ever understood the stakes in the game, or how far Russian subversion of our system had got – I would argue that already in the 2016 presidential election, or Brexit, in the same year, Russian political technologies were already deployed to devastating effect in support of Russian interests and the ultimate victory of kleptocracy/sovereign democracy over Western Liberal Market Democracy. One might well ask is it already too late given the rise of the Afd, and Le Pen, et al, and potential for Trump to return to finish the job in the US.

True, I think the Biden administration finally woke up to the threat from Russia, at least to Ukraine, with Russia's military build up over the course of 2021, and then with the full scale invasion of Ukraine in February 2022. Outing Russia in its mission to invade Ukraine was a brilliant PR move by the US – it was the last hope perhaps of averting the invasion, but by this time it was perhaps already too late, as years of cow towing to Moscow at the expense of backing Ukraine's defence meant that Ukraine was by then woefully underequipped to deter the inevitable Russian invasion.

Russia invaded Ukraine in 2022 because Putin fundamentally did not accept Ukraine's right to exist, and Ukrainians' identity separate from Russians – and the Nato enlargement threat was the bluff/excuse/smokescreen. But Russia invaded also because it could, because Putin expected no Western response and assumed a speedy Ukrainian defeat because Moscow had seen the timidity from the West in failing to supply Ukraine with the weapons to defend itself. Indeed, Russia and the West, and perhaps the Ukrainian leadership itself, did not think Ukraine could fend off a Russian invasion. The widespread assumption was that the war would be over in weeks, and result in an overwhelming Russian victory. The only defence for Ukraine was deterrence, but the West had left Ukraine brutally exposed there with little real signalling to Russia as to the real negative consequences of such an invasion. Putin invaded because he expected a speedy victory and little international consequences. That was a seismic and catastrophic failure of Western leadership.

Thank god for the bravery of Ukrainians – they were the deciding factor in the early weeks of the invasion, plus the arrogance and incompetence, corruption, etc of the Putin regime.

But the West still did not learn, even with the Ukrainians appealing for advanced weaponary to defend their country. Yes, there were real concerns at this point as to the willingness of Putin to escalate – did he have escalation domination, and was he willing to do literally anything to take Ukraine? Quickly we learned though that he did not, by going through the gears of supplying more javelins, manpads, then T72s, Mig29s, HIMARS, Lepards, ATACMS, and eventually F16s, that Putin set red lines but did not keep to them. There was a worry that Putin would resort to WMD around the time of the siege of Azovstal, but he did not, and I think the West should have learned two things from this, which demonstrated Putin's own constraints:

First, on WMD, and broader escalation, I think that Putin values the relationship with China. And herein, Xi I think was discomforted with Putin's invasion of Ukraine as it risked destabilising global markets and by so doing the globalisation driven ascent to economic hegemony that China so desired. So I think Xi set constraints in Russia of no first use of WMD, or any sanctions response which would have potentially destabilised global markets. Indeed, in response to aggressive Western sanctions, Russia had an array of options across commodities to cause strain on global markets, but failed to use its leverage. And China's leverage here is that ultimately

> "One can see the failures very early on from the Biden administration, and particularly from its national security leadership in continuously failing to read Putin"

the Russian economy depends on markets in China for its commodities. Russia was not willing to go against the ultimate strategic interests of its paymaster, China.

Second, I think we learned in Nato going thru the gears of weapons supply to Ukraine that Putin is actually scared of a direct conventional war with Nato. And I think here he realises that because of Nato's huge technological superiority (as evidenced through the war in Ukraine), that Russia would lose any such war very quickly. Perhaps he realises that in any such war, a speedy conventional Russian defeat would see it forced to fall back on the nuclear defence but then capped by constraints from China. There are obviously stories that the West warned Putin in 2022 of a massive Nato conventional strike in Russia in response to a first use of WMD in Ukraine – perhaps here it is a combination of the threat from Nato and the restraining force of China. But net net, when it comes to the warnings of retaliation from Putin over the Western supply of F16s to Ukriane or now permission to use long range missiles against targets in Russia, the same Russian red lines are not serious. Putin is not going to attack Nato in response or resort to WMD, as that would be both an acceptance by him of weakness and failure (in Ukraine) but also would hasten his own defeat by bringing in Nato and China against him.

The recent debate about green lighting long range missile use for Ukraine, just affirms to me that the Biden administration, and absolutely the German government, have still not learned much about Putin from the two and a half years of this war. But spelling it out to them, in simple terms, Putin is a bully, who only respects force. You show him weakness and he will exploit your weakness.

Putting all this together the West should focus on providing Ukraine with the full range of conventional weaponary needed to win the war. This will send the best message possible to Putin that he cannot win the war, and will force him to negotiate peace – from a postition of Ukrainian strength.

Lack of leadership on sanctions

The West has gone a lot further on the sanctions front than I think anyone, including Putin, imagined in the run up to the full scale invasion. But the reality is that sanctions have been still too timid and slow moving to have enough effect. Yes, sanctions are only one part of the toolkit of statecraft, but we could and should have done much more. Partly I think the mistake made by the US, in particular, was this desire to ensure Western unity, and to try and bring all Western nations on board. There has also been a reluctance to take pain by the West. Hence there has always been a long negotiating process to minimise the damage to individual Western economies, and companies (many lobbied hard against), and hence we ended up with sanctions by the path of most resistance. Too little, too late, often, and giving Russia lots of routes to circumnavigate sanctions. The reality is the question should have been, is Russia an existential threat to Western national security – answer, absolutely. Then how can we hit Russia hardest, and to change behaviour as quickly as possible, and if so we need also to be prepared to take some pain. And in the end, forget about Western unity, the US is the dominant economy in the Western world, and everyone complies with the US Treasury. The US should have just said, this is a national security issue, this is what we are doing, you have to follow, or else. You are either with us or against us. Then obviously the US, and it's allies, should have followed up more aggressively with secondary sanctions ensuring that the likes of China, India, Turkey, et al did not try and circumvent the sanctions for their own benefit.

Lack of leadership around financing Ukraine

Linking sanctions and financing of Ukraine, the issue of making Russia pay and the adequate funding of Ukriane to win are interwoven through the issue of immobilised Russian assets – particularly the $330bn in immobilised Russian assets in Western banking systems.

On the sanctions list, perhaps if Russia thought it would have to pay for the destruction wrought in Ukraine, through the loss of the $330bn in immobilised Russian assets, maybe it would have been less willing to cause the destruction.

"The reality is the question should have been, is Russia an existential threat to Western national security – answer, absolutely"

On the financing front the data is the data. Western funding for Ukraine has been running at around $100bn a year since the full scale invasion. That's enough funding for Ukraine to just about stay in the war, but I would argue that Ukraine needs more like $150bn a year to win. I would argue that the threat from Russia to Western security is such that funding Ukraine to the full $150bn should be a Western public good, payable by Western taxpayers – and it's only a few percentage points of Western GDP. But I get the global cost of living crisis and competiting demands for government spending in the West. In reality the West has not been able to increase spending to the $150bn a year level for Ukraine to win, and given political strains in the Western alliance – the $61bn stuck in the US Congress for months – funding has at times dropped well below the $100bn annualised for Ukraine to win, and at those times Ukraine has tended to be pushed on the back foot in the war. It would be nice if Western leaders were honest with their electorate and explained that this is the Russian threat, Ukraine is the best means to defeat Russia and alleviate the risks, and this is the cost ($150bn a year). Unfortunately our leaders have neither adequately explained the threat or how the funding is to be met. As is I don't think Western taxpayers are willing to write a cheque for $100bn a year or $150bn even. And as the war likely extends into 2025, and with the risk of a Trump presidency late this year and US funding (40% of total Ukraine funding), I think Ukraine will face a financing cliff next year.

Now guys like me, and others like Zyskind, Zelikow, Zoellick et al have warned for more than two years about the funding crisis and identified the only means to fund Ukraine adequately to win is to use immobilised Russian assets – the $330bn in CBR assets. But our calls have gone on deaf ears and been countered by European governments (Germany, Belgium and Italy) which have stalled the process of freeing immobilised Russian assets for Ukrainian use. Their arguments against are weak, and their opposition fundamentally reflects oppositon from business vested interests, rather than the interests of their own taxpayers. But let's not beat around the bush, if Ukraine is not adequately financed it will lose the war and the costs then of an empowered revanchist Russia will be multiple times higher for the Western alliance and for Nato. But herein the same European leaders who misread Putin for the past few decades are now the same forces which are blocking the use of immobilised Russian assets for Ukraine.

What is needed here again is for the US to step up and force the issue and threaten Western institutions with sanctions unless they sign off on the decision to allocate the full $330bn in immobilised Russian assets.

I know here there is a wheeze to trying and structure bonds using the interest flow from immobilised Russian assets, but the $50bn planned does not touch the sides really in terms of Ukraine's annual $100-150bn financing needs. It's a diversion, arguably which has stalled the initiative to use the full $330bn in immobilised Russian assets.

Looking across the issues above, we see a fundamental problem of a lack of Western leadership in addressing the threat from Putin, and in providing Ukraine with the resources to win the war – which is is in our fundamental security interests. Europe is obviously weak and divided, as a result of populism and the rise of far right and far left political forces – fanned and funded by Putin. The US ultimately should have provided the leadership but the Biden administration has fallen short. ●

***Timothy Ash** is the senior sovereign strategist at BlueBay Asset Management in London. This blog first appeared on his substack.*

COMMENT

Eurasian Development Bank and FONPLATA call for tailored approaches to expanding MDB lending capacity

bne IntelliNews

The Eurasian Development Bank (EDB) and South American FONPLATA Development Bank have jointly published a policy paper titled "One Size Does Not Fit All – Analyzing the Applicability of Options for Expanding Lending Capacity Across MDBs", which calls for more customised strategies to enhance the lending capabilities of multilateral development banks (MDBs).

The policy brief was presented under the aegis of T20, a G20 engagement group that brings together global think-tanks and research centres.

The research, led by Evgeny Vinokurov, Vice Chairman and Chief Economist of the EDB, and Oscar Llamosas, Vice President for Strategic Development at FONPLATA, focused on regional and sub-regional MDBs, whose specific needs and capacities often differ significantly from larger global institutions. The authors examined how varying approaches to capital mobilisation could be applied across MDBs, highlighting the importance of tailoring strategies to fit the unique characteristics of each institution.

"The G20 Independent Review of MDBs' Capital Adequacy Frameworks estimates that MDBs will need to provide an additional $260bn in annual official financing to achieve the Sustainable Development Goals by 2030," the report notes. This would require both an increase in available capital and more efficient utilisation of MDBs' resources.

Unique role of regional MDBs

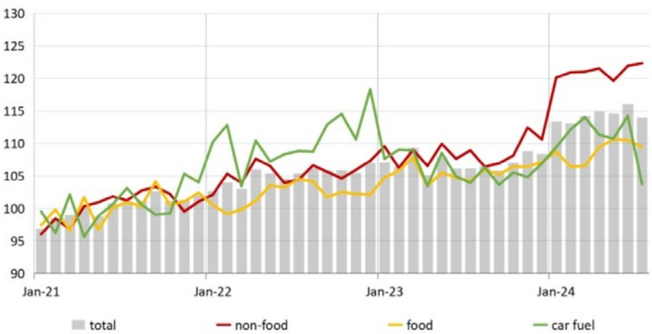
Vinokurov underscored the advantages that regional and sub-regional MDBs bring to the development landscape, noting their flexibility and deep understanding of local conditions. "Regional and sub-regional MDBs are generally more flexible, have a better understanding of the conditions of member countries and regions, and can therefore be very helpful to their member states. Adequate capital is a major prerequisite along this way," he said.

The policy paper proposes several strategies for capital enhancement, including increasing shareholders' capital, expanding membership to include both regional and non-regional countries, attracting institutional investors, and exploring partnerships with other MDBs. It also examines more unconventional methods, such as channelling IMF special drawing rights (SDRs) to MDBs, though these have yet to be fully tested.

The recommendations encourage G20 nations to support MDBs in adopting a "lending-capacity-expansion strategy consistent with their specific strengths and weaknesses" in order to mobilise more resources for their member states. ●

The full policy paper can be accessed here:
www.t20brasil.org/media/documentos/arquivos/TF03_ST_02_One_Size_Does_Not_F66e19a5be3588.pdf.

Romania: Retail Sales Index [2021=100; seasonally, workday adjusted]



Sales of non-food goods in Romania soar to new record in July

The volume of retail sales in Romania rose by 8.1% y/y in July slightly slower compared to the 9.8% y/y advance in Q2, dragged down by sluggish sales of car fuels (0.6% y/y) but substantially driven by the sales of non-food goods (14.5% y/y) that reached a new record when expressed in seasonally adjusted terms.

Private consumption in Romania remains robust, fueled by the significant advance in net wages (by 6.5-8.2% y/y over the past three quarters). The pass-through ratio from retail sales to GDP growth is, however, modest due to the reliance on imported consumer goods in a multitude of segments.

Russia monetary policy rate vs CPI inflation y/y

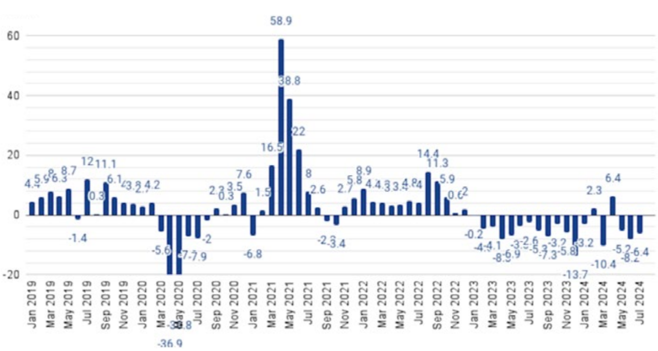
Source: CBR

Russia's central bank surprises market with 100bp rate hike to 19%

The Central Bank of Russia (CBR) surprised the market with a surprise 100bp hike on September 13 taking the prime interest rate to 19%.

The decision comes as inflation at 9.1% is thought to have peaked and the overheated economy is cooling after the CBR teamed up with the government to use non-monetary policy methods to reduce the inflationary pressures.

Hungary industrial production y/y



Source: Hungary state statistics agency

Hungary's automotive industry extends decline as export markets struggle

Output of Hungary's industrial sector fell 1.3% y/y in July and by 6.4% when adjusted for the number of workdays, the Central Statistics Office (KSH) confirmed in a detailed release of data on September 13.

Domestic industrial output has essentially stagnated or slightly declined since mid-2022. Short-term production prospects remain bleak, with economic indicators across Europe showing only faint signs of recovery, analysts said. The 6.4% decline was the steepest drop among EU members, but two extra days in the base period explain the big gap in the two figures

Russian population unhappiest it has been in a decade

Eight out of ten (78%) of Russians consider themselves to be relatively happy, according to the Russian Public Opinion Research Centre (VTsIOM). However, the overall happiness index has dropped to its lowest point since November 2014, TASS reported on September 16.

The data shows a noticeable shift in sentiment over the past three months. "The share of those who consider themselves absolutely happy has decreased to 32%, while those who describe themselves as rather unhappy has increased to 12%," the pollster added.

Ukraine has both the highest mortality rate and the lowest birth rate in the world

Ukraine currently holds the grim distinction of having both the highest mortality rate and the lowest birth rate in the world, according to the latest data from the US Central Intelligence Agency (CIA) factbook.

The updated World Factbook reports that Ukraine's death rate stands at 18.6 per 1,000 inhabitants, placing it at the top of the global rankings. Lithuania follows with 15.02 deaths per 1,000 people, while Serbia is third with 14.9. In contrast, Qatar has the lowest mortality rate, recording just 1.4 deaths per 1,000 inhabitants.

Additionally, Ukraine has the lowest birth rate worldwide, with only 6 births per 1,000 people. The French territories of Saint-Pierre and Miquelon occupy the second-lowest spot, with a birth rate of 6.4 per 1,000 people. Niger, by comparison, has the highest birth rate at 46.6 births per 1,000 inhabitants.

In 2024, Ukraine's mortality rate is expected to be three times higher than its birth rate, with Dnipropetrovsk Oblast and Kyiv recording the majority of both newborns and fatalities.

As *bne IntelliNews* reported, the war in Ukraine with Russia has caused a demographic catastrophe that is the worst example of a wider demographic crisis that is sweeping Europe and will take Emerging Europe population levels back to the early 20th century.

"The ever-present proximity of death or Russian occupation, family separation, and financial as well as physical insecurity is having a dire effect on Ukraine's already-declining birth rate," the World Bank said in a report last year.

Ukraine's birth rate has already plummeted to a 300-year low as the country's population collapses. Ukraine's population shrank to 29mn last year from 45mn pre-war, according to Ukraine Business News, with just 187,000 births recorded (including in Russian-occupied territories). This is the lowest annual figure in recorded history over the last 300 years, exacerbating an already dire population catastrophe facilitated by economic turmoil and war.

Ukraine's demographic crisis dates back to the Soviet collapse in 1991, when the country's population stood at a record 51.9mn. Economic crises and labour migration saw the country's total fertility rate plummet to 1.4 births per woman (well below the replacement level of 2.1) by 2022 and possibly as low as 0.7 by the following year, according to Ukraine's Institute of Demography and Social Studies.

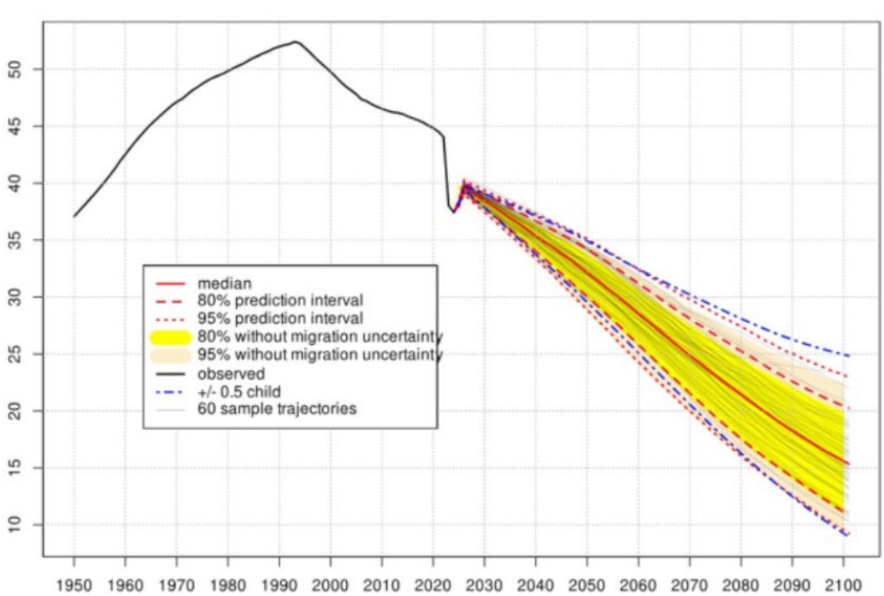
And the population will not recover quickly even if the war ends tomorrow. The latest UN median forecast for Ukraine's population by 2100 is for it to more than halve from its pre-war levels to a mere 15.3mn people, according to UN's 2024 Revision of World Population Prospects.

"The popular TV ad of the early 90s "We are 52mn" used to be part of the identity of Ukrainians of my generation. Now even the most optimistic scenarios predict half as many. "Towards the abyss" visualised," Volodymyr Ishchenko, a research associate at the Institute of East European Studies at the Freie Universität Berlin.

Demography is a problem across all of the Former Soviet Union (FSU) and Europe, but ironically, Russia is performing the best of any major economy at the moment, thanks to Putin's babies, consistent natal and maternity reforms that the Russian president launched during his first term of office in 2000. The Kremlin has also been promoting larger families with a raft of generous financial and tax benefits over the last two decades.

Russia's fertility rate of 1.49 is one of the higher rates in Europe and continues to rise. The military Keynesianism boost to the Russian economy, coupled with record-high real disposable incomes, has fuelled a consumer boom and helping fertility, although there are increasing signs the war bump effects are beginning to wear off now. ●

Ukraine: Total Population



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United Nations, DESA, Population Division. *World Population Prospects 2024*. http://population.un.org/wpp/

Newsletter

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