

Crimea Transition to Have 'Serious Impact' on Russian Economy

By [The Moscow Times](#)

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Looking down at the Black Sea from the Sarach headland on the Crimean peninsula's hilly south coast near Foros.

It will replace Egypt as a tourist hotspot, its offshore oil and gas reserves will cement Russia's position as the world's top energy producer, and its spas will revive the state sector's weary workforce. At least, that is how Russia presents Crimea.

Many in Russia hope the annexation of the southern Ukrainian region will offer only benefits and an opportunity to celebrate the "return home" of Russia's more than 1 million "brothers" after being handed to Ukraine 60 years ago.

But the joy they felt when Crimeans voted resoundingly to join Russia in a referendum on Sunday may be tempered when it comes to the tough budget decisions needed to prop up an economy dependent on Ukraine for energy, water and food.

Russia's chief cheerleader on Ukraine, parliamentarian Leonid Slutsky, would not be drawn into listing the potential pitfalls of welcoming the region of 2 million people into the Russian Federation. He preferred to focus on the winners.

"Those who most benefit ... are the simple people, the simple Crimeans who today are completely different from those people I saw two weeks ago, with their faces lit up, kissing their ballot papers," Slutsky said from the capital Simferopol.

"People are happy ... they are protected, they will return to the country where they wanted to be for at least the last two generations, and finally because historical truth, this historical justice, will prevail," he told Ekho Moskvyy radio.

What they regard a historical justice, making up for Soviet leader Nikita Khrushchev's decision to hand over Crimea in 1954, will also return a favorite holiday destination, where Soviet industrial workers were sent to take in the sea air.

After Crimea's parliament voted on Monday to nationalize the region's main energy company, Chornomornaftogaz, Russia may be in a better bargaining position to wrest offshore and shelf rights in the Black Sea.

But while the vote plays on Russia's emotional ties to the Black Sea peninsula, few are considering how much money may be needed to turn around a region of shabby hotels, poor service and a large black economy.

Crimea, a lush region known for its palm-fringed seafront boulevards and rocky hills, is subsidized and depends on Ukraine for 85 percent of its electricity, 90 percent of its drinking water and much of its food.

Karen Vartapetov, an analyst at Standard & Poor's rating agency, calculated that Moscow would need to pay 38 billion rubles (\$1 billion) a year to bring Crimea's per capita budget revenue to the same level as Russia's poorest regions, such as North Ossetia and Kabardino-Balkaria in the restive North Caucasus.

'Crimea Weekend' Hurts

It would mean lifting pensions for about 560,000 pensioners from an average of \$150 a month to Russia's minimum of \$180. The average wage in Crimea stands at \$270 a month, compared with \$660 just over the border in Russia's Krasnodar region.

Russian officials say they are ready to send anywhere from 30 billion to 40 billion rubles in financial aid to Crimea to help it move under Russian control — a process Deputy Finance Minister Sergei Shatalov said would "have a very serious impact."

"There will be changes in tax laws, the issue of forming a customs service, an internal revenue service, and the registration of legal entities and individuals, inventories and rules to adapt to the Russian tax system," he told reporters.

"I think it will require some time, perhaps there will be a period of transition. I do not rule out a special tax regime."

It will all happen when Russia's economy is weakening at an accelerating pace, partly because of its actions in Ukraine, where Russian forces have seized Crimea and Moscow supported the referendum in which official results showed almost 97 percent voted in favor of joining Russia.

According to economist Jouko Rautava, of the Institute for Economies in Transition at the Bank of Finland, economic growth in Russia in 2014 could dip below 1 percent after the "Crimea weekend" — well short of the Russian Central Bank's forecast for 1.5 to 1.8 percent expansion.

That will mean federal and regional budgets will have to stretch further to cover Putin's orders to provide better wages for public sector workers, benefits for mothers and infrastructure development.

"The problems in the [Russian] regions are getting worse, and there are about 10 to 15 regions which urgently need financial aid to fulfill Putin's orders," said Vartapetov.

"This is a question of priorities; to help the Russian regions or send that help to somewhere else, to another territory," he said, adding that Crimea could cost less to Russia if it kept taxes on profits like other Russian regions, rather than sending them to the center as it does now.

Turning the Tide

Vartapetov said at least 10 Russian regions have debts of 100 percent of their revenues.

"Access to the debt markets for them is extremely difficult, and they can only hope for help from the federal budget," he said.

"And the regions will need more every year because the economy is slowing, tax collection is stagnating and expenditure is growing; deficits are just widening."

Some analysts say that over time, the potential for domestic resentment will grow, unless Crimea offers Russia something in exchange.

Its offshore oil and gas reserves could extend Russia's energy reach, and Crimea's new leaders have already suggested Gazprom should buy its energy major Chornomornaftogaz.

But with Western sanctions targeting those who have "undermined the territorial integrity" of Ukraine, Russian companies could come under pressure if they start taking over formerly Ukrainian firms.

Some analysts say Russia may resort to a tried and tested way of solving financing conundrums — by bringing in the oligarchs.

After funding much of the construction of Russia's Winter Olympic venues in the Black Sea resort of Sochi, widely expected to have cost more than \$50 billion, some Russians suggest Putin will persuade them to stump up cash again to transform Crimea's tired resorts into world-beating tourism hubs.

"Crimea would be another headache and a new 'Sochi Olympics' for the Russian oligarchs, who will be forced once again to plough their money into a Kremlin-designed project," said

a source close to state energy company Rosneft.

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