

## Economic crisis in Transnistria as a chance for the EU diplomacy

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**The economic situation in Transnistria has deteriorated suddenly in the last quarter of 2008, causing serious financial difficulties for the separatist Pridnestrovian Moldavian Republic. The crisis may deepen the divisions existing within the Transnistrian business and political elite, and dent its pro-Russian orientation. This would be a perfect opportunity for EU diplomacy to reinvigorate stalled efforts to resolve the frozen conflict between Moldova and the Transnistrian separatist regime.**

### History of the conflict

The conflict between the Republic of Moldova, with its capital in Chisinau, and the Pridnestrovian Moldavian Republic, with the capital in Tiraspol, stems from the split within the party elite of the Moldavian Soviet Socialist Republic (MSSR) which occurred during the period of Mikhail Gorbachev's reforms. The republican nomenklatura divided roughly along linguistic and political lines with Romanian-speakers embracing the postulates of the Popular Front of Moldova (elevation of Romanian as the dominant official language of public life and separation from the USSR), while Russian-speakers defended the dominant status of the Russian language and the integrity of the USSR. At the instigation and with assistance of the Soviet Union's central authorities, the Russian-speaking nomenklatura established, in opposition to the the Chisinau-based government of Moldova, the Pridnestrovian Moldavian Republic (PMR), led by Igor Smirnov. After Moldova had declared independence in August of 1991, in September of the same year the PMR proclaimed its accession to the USSR and manu militari extended its rule over the part of the MSSR's territory located on the left bank of the Dniester. Unrecognised by the international community, the Tiraspol regime has nevertheless been informally supported by Russia, which in the summer of 1992 intervened militarily on Tiraspol's side in the armed conflict with the Republic of Moldova. Since then Russia has been informally protecting Transnistria and maintaining a military contingent on its territory, which has been acting as a peacekeeping force under the 1992 ceasefire accord and protecting the military depots left in Transnistria by the Soviet army. A negotiating mechanism has been developed under the aegis of the OSCE. Since 2005 it has been operating in the so-called 5+2 format, with Moldova and the PMR as the sides of the conflict, Russia, Ukraine and the OSCE as mediators, and the EU and the USA

as observers. The main stumbling block have been the demand of the separatists to be recognized by Kishinev as a fully independent and equal party to the negotiations. Tiraspol bases this claim on a 2006 referendum (which however was not recognised by the international community). The negotiations in the 5+2 format were *de facto* broken off in March 2006, and since then it has proved impossible to revive them.

## The European Union's interests

Since Brussels started aspiring to create an area of stability and prosperity around the European Union (as expressed through the European Neighbourhood Policy adopted in 2003 and last year's Eastern Partnership initiative), and since Romania became an EU member state, the Transnistrian issue has also become the European Union's problem. The EU has been gradually stepping up its involvement in the resolution of the conflict between Chisinau and Tiraspol. However, it has done so mainly by supporting initiatives proposed by others (such as the initiative by the Dutch OSCE presidency in 2003, and Ukraine's Yushchenko Plan in 2005). These efforts, however, proved futile due to the resistance of the separatist

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regime in Tiraspol, backed, for geopolitical reasons, by the Kremlin.

The European Union is paying a high price for the continuing *de facto* division of Moldova and the existence of an internationally unrecognised quasi-state in Transnistria. Firstly, the very existence of an unrecognised regime and of a territory

with unclear international status just outside the EU's borders is a destabilising factor. It creates a kind of 'corridor' through which goods, drugs and migrants may be smuggled into the EU. Secondly, the unregulated conflict with Tiraspol has been hindering internal reforms in the Republic of Moldova, impeding its integration with the EU. This is because the conflict has been distracting the attention and energy of the Moldovan political class away from internal problems and have been creating opportunities for 'grey' business activity and corruptive links, as well as adversely affecting ethnic relations. It has also made Chisinau largely dependent on Russia by limiting its options in international relations. Thirdly, the frozen conflict has offered the Russian Federation an opportunity to pursue its revisionist great power agenda. Finally, even though the risk of a renewed armed clashes seems to be minimal at the moment, it might potentially materialise in the future. The ruthlessness shown by the Transnistrian elite in both politics and business leaves no doubt that it would not hesitate to provoke armed incidents if it saw some benefit in this.

The European Union should therefore be interested in resolving the Transnistrian issue as soon as possible. By ushering in a resolution of the conflict, the EU would demonstrate its capacity to take effective international action and tackle regional conflicts.

The current deep economic and financial crisis which has hit the unrecognised republic during the last few months offers a good opportunity for a more energetic EU initiative on Transnistria. There are many indications that the crisis will worsen. The complete paralysis of the Transnistrian economy and a breakdown of the financial system cannot be precluded.

## Symptoms of the crisis

Transnistria started to experience the consequences of the global crisis in the last quarter of 2008. Its economy, dominated by a handful of large heavy-industry companies producing mainly for export, turned out to be extremely vulnerable to the slowdown in global markets for metallurgic products and cement. In October 2008, the value of Transnistria's exports had already dropped by half (to US\$41.4 million, compared to the monthly average of US\$82.4 million between January and September)<sup>1</sup>. This entailed a decrease in industrial production by 20–30% in the fourth quarter of 2008, and in sales by as much as 40–60%<sup>2</sup>. The ten largest companies which the Transnistrian budget relies on have been hit most severely by the crisis; for example, the Ribnitsa steelworks which accounts for 50–60% of Transnistria's exports and around 30% of budget revenue reported a four-fold drop in sales in the fourth quarter, and cut its production by half. The situation is similar in the second largest industrial establishment, the Ribnitsa cement plant. Prices of the main export commodities have decreased by half. As a result, companies have begun sending

**The economic crisis can fatally undermine the Transnistrian budget for the current year.**

workers on forced unpaid leave, and are predicting layoffs in the near future. The situation has been exacerbated by the nearly complete two-week interruption of gas supplies to Transnistria during the Russian-Ukrainian gas conflict. Small businesses, which are usually faster to react and adjust to crisis situations, account for only 13% of Transnistria's economy. Moreover, Transnistria is burdened with a debt of around US\$2 billion.

The crisis in industry has had an immediate effect on the PMR's budget revenues which shrank by 20–30% in the last quarter of 2008. If a similar trend continues this year, then the 2009 budget which the Transnistrian government adopted in December will soon break down. When originally adopted, the budget had already envisaged a deficit of around US\$100 million (around 10% of the GDP) while projecting a 40 percent (nominal) increase in budget revenue over the previous year<sup>3</sup>. It has now become clear that this assumption was totally unrealistic.

Due to decreasing budget revenue, in December last year the government stopped financing all budget lines, except for salaries and welfare benefits. In spite of this measure, it ran out of funds to pay pensions and had to borrow around US\$1 million from the Central Bank<sup>4</sup>.

All this indicates that the economic situation for people in Transnistria will continue to deteriorate. They will now face the likelihood of losing their incomes as well as delays in pension and benefit payments, in addition to high inflation (26% between January and September 2008, with food prices rising even faster – by 74% in the case of meat, 30% in the case of milk and 300% in the case of rice)<sup>5</sup>.

The Transnistrian media are sounding the alarm and predicting a culmination of the crisis in spring 2009, with a breakdown of the financial system and the full paralysis of the economy.

## Calls for external assistance

The Transnistrian authorities do not know how to combat the crisis, nor do they have sufficient funds to do so. In this dramatic situation, on 19 December 2008 the Transnistrian parliament requested financial assistance from the Russian government. (Last year, Russia provided Transnistria with around US\$30 million of aid). Five days later, the parliament called on the Ukrainian parliament to restore the border regime that had been in place before March 2006. This would allow Transnistrian firms to export goods through Ukraine without be-

<sup>1</sup> INFOTAG (8.12.2008).

<sup>2</sup> ADEPT, e-journal, year VI, issue 129, 1-31 December 2008, <http://www.e-democracy.md/en/e-journal/20081231/>

<sup>3</sup> *Pridnestrov'e* (13 November 2008) <http://www.pridnestrovie-daily.net/gazeta/articles/view.aspx?ArticleID=11630>

<sup>4</sup> INFOTAG (17 December 2008).

<sup>5</sup> <http://www.regnum.ru/news/1082159.html>

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ing subject to the control of the Moldovan customs authorities and thus would widen the possibilities for illegal or semi-legal trading schemes on the Transnistrian section of the Ukrainian-Moldovan border.

However, the current Ukrainian government will most probably deny the request. It is interested neither in offering political support to the separatist, pro-Russian regime in Tiraspol, nor in creating better

opportunities for smuggling (as that would entail losses for the Ukrainian budget as well). As regards Russia, it will most probably offer Transnistria some financial support, but it is unlikely that against the background of declining oil and gas prices, the Kremlin should be so generous as to offer any major help to its Transnistrian *protégées*.

## An opportunity for the European Union

The dramatic economic and financial situation in which Transnistria finds itself offers an opportunity to EU diplomacy. The European Union should take the initiative by intensifying its informal consultations with Transnistria in order to persuade the regime to accept reunification with Moldova while maintaining broad autonomy for Transnistria. It should resort to a classic carrot and stick method. On the one hand, it should promise an ad hoc economic and financial aid for Transnistria and access to the EU assistance programmes within the framework of the European Neighbourhood Policy and the Eastern Partnership, and on the other, threaten to bar Transnistrian companies from the EU market (the EU accounts for 35% of Transnistria's exports). The European Union could invoke here the fact that most of the companies in question have been illegally privatised by the Transnistrian authorities.

An EU initiative at this moment could find a positive reception in the Transnistrian business and political elite, which appears to be starting to doubt the prospect of assistance from Russia<sup>6</sup>.

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Firstly, the Transnistrian political and business leaders are aware that Russia, itself affected by the financial crisis, will not be a willing and generous donor to Transnistria. Secondly, they are disappointed with Russia's refusal to recognise the independence of Transnistria while it did grant recognition to the autonomous republics in Georgia<sup>7</sup>. Thirdly, the Transnistrian elite

must have noticed the complete indifference that Russia showed to the plight of the Transnistrian population during the recent gas crisis, when people had no gas at all for two weeks.

It is very likely that the economic problems will deepen the political divisions which have existed within the Transnistrian establishment for a long time. In a situation in which the Smirnov regime proves unable to support the exporting companies, those companies may become inclined to look for political solutions other than simply preserving the status quo.

A possible EU initiative would also benefit from the fact that the Moldovan president, Vladimir Voronin, is now particularly keenly interested in resolving the Transnistrian problem. The main reason for this is that his second and last presidential term is drawing to a close, and the future of his political career now hinges on the results of his party (the Communists) in the April parliamentary elections. Even though the Communist party controls most of the media and can use the state apparatus (in particular, the courts, the procuracy, the police

<sup>6</sup> N. Morar', 'Volna krizisa dokatilas' i do Pridniestrovia', *The New Times*, 1 December 2008.

<sup>7</sup> A.Safonov, 'Chto budet s Rodinoy i s nami?', *Novaya Gazeta*, 24 December 2008. <http://novaiagazeta.org.ru/index.php?cstart=3&>

and the tax inspection authorities) in the election campaign, it cannot be sure of a victory. In 2007 the Communists reported a poor showing in the local elections, and in 2008 were defeated, albeit minimally, by a coalition of regional forces in the elections to the parliament of the Gagauz autonomous region.

Unifying the country, or at least creating prospects for unification, would improve the Communists' chances of retaining their parliamentary majority and thus staying in power. Besides, Voronin wishes to gain the laurels for uniting the country – he clearly has a personal attitude to the issue, which is partly because he himself comes from Transnistria. In such circumstances, the EU diplomacy would have good chances of winning Voronin over to its initiative.

To sum up, the economic crisis in Transnistria, combined with the internal situation in Moldova and the Kremlin's financial difficulties, create favourable conditions for an attempt to resolve the Transnistrian conflict once and for all. For the European Union, this is a perfect opportunity to solve one of the 'frozen' but potentially still dangerous conflicts in its immediate neighbourhood, and to demonstrate its ability to take effective international action.



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