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Railroading

The Putinization of Estonia

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Railroading BRS

The Putinization of Estonia: Russian money and influence

By Jüri Estam

Estonia is like an atoll in the middle of the ocean, where the tides roll in and out—first from one direction and then from another. By tides, I mean Estonia’s fortunes in war and peace. Small countries in sensitive geopolitical locations have a harder time being masters of their own fate than large countries and isolated lands. Estonians have periodically experienced wrenching political and economic transformations.

In a study titled, “Breaking Away from Russia—Economic Stabilization in Estonia 1918-1924,” the scholar Jaak Valge wrote of an extremely difficult but fascinating and colorful period that arrived after Estonia’s 1918-1920 War of Independence. This was a time when the flow of Estonia’s economic rivers was literally reversed. Disengagement from Bolshevik Russia meant severing the countless veins and arteries that connected Estonia to Russia’s economy, and grafting them to new Western partners. For several years, Estonia remained an impoverished conduit between East and West, at a time when Soviet Russia needed an outlet for laundering her huge reserves of gold and other riches. The People’s Commissar of Finances, Isidor Gukovsky, while in Tallinn to coordinate these activities, wrote that Estonia would again become part of Russia when the Bolsheviks wanted it. “But at the moment,” he wrote, “we need its ridiculous independence.”

Adventurers and swindlers from afar gathered here. A French journalist described 1921 Tallinn as an “international sewer.” Jaak Valge referred to an “eastern trade disease” that prevailed among many key figures in Estonian political and economic life. Many politicians took questionable loans to get in on the eastern trade, which dried up just as suddenly as it had started. Valge wrote that “...the revenue from the East had a net negative effect on the Estonian economy,” and described a crisis in business and governance values—one that “deformed the political relations of the country, but also made disengagement from Russia all the more painful.”

Things gradually improved in Estonia. By the late thirties, things were going pretty well. Then came sudden annexation by the USSR in 1940. This time, Estonia’s veins and arteries were severed from the West. The Kremlin seized holdings, outlawed private property, nationalized enterprises, and introduced central planning. Human rights and freedoms were suspended, and fear descended upon the land.

Fifty years later, the Baltic states regained their independence. Once again, it was time to try to make the rivers reverse their flow. Extensive privatization was undertaken. In February of 2001, when much of Estonia’s infrastructure was already in the hands of new owners, the Mayor of Tallinn, Jüri Möis, met secretly in London with Sicilian-born Giovanni Sposato, to discuss the possibility of Sposato’s investing 1.7 billion kroons (109 million euros) in the privatization of the Estonian rail system. The Estonian media got wind of the episode. It turned out that the offer was frivolous, and the entire affair caused not only a setback of several months in the efforts to privatize the national railway system, but also embarrassment for the Estonian side. Sposato, a rakish figure who at one point set fire to the car of a girlfriend who spurned him, was later arrested in Estonia, deported in 2003, and banned from reentering this country. He is but one figure in the rogues’ gallery of the era of privatization. Though, more precisely, along with the carpetbaggers came some serious newcomers.

If there are losers in this story, they are the Estonian people.

Estonian Railways finds a buyer

In August 2001, a consortium called Baltic Rail Services (BRS) succeeded in purchasing a 66% interest in Estonian Railways, with the remainder staying in the hands of the Estonian government. Two American firms were among the purchasers in the form of Rail World Inc. and Railroad Development Corporation. The government then in power, headed by Mart Laar, regarded the presence of American capital in Estonia as “soft security.” Since it didn’t look like NATO was planning to station troops here soon, this was a second best option for helping cement Estonia to the West.

The American railway men who arrived set out to cure the hand-me-down Soviet-era ills and inefficiencies of Estonian Railways and to turn a profit. Based on conversations I've had, they sensed that they were also idealists, and saw themselves helping Estonia to return to the free world.

BRS had lots of ideas. They considered overhauling locomotives here and wanted to rent powerful American locomotives to other countries from their Estonian base. As recently as 2005, BRS set up an office in Moscow to try to help route an increasingly sophisticated mix of cargoes all the way from Asia to the West via Estonia. The other moneymaking idea was to conduct an initial public offering of Estonian Railways stock, but it was never to be.

Luck was not with the Americans. Six months after their arrival, the Laar government left office along with its free enterprise credo, and a new coalition with the Centre Party in a lynchpin position took over. Edgar Savisaar, the populist leader of the Centre party, is the man characterized by Mel Huang as "illiberal" in a recent issue of *City Paper*. Mr. Savisaar, who has been the Estonian Minister of the Economy and Communications for several years, has been accused of being the "long arm of Russian power" in Estonia by such people as his own fellow minister Rein Lang. The Centre Party maintains a controversial cross-border partnership with Unified Russia, the political party most closely associated with the Russian president Vladimir Putin. Mr. Savisaar engages in pork-barrel politics (a practice he is not alone in) and vote-buying tactics. One example of many: According to the daily *Postimees*, while campaigning in the settlement of R pina, Centre Party candidate Heimar Lenk showed voters checks made out to the local Pensioner's Club for the purchase of computers in the sum of a hundred thousand kroons, which was just one of several such promises to pay. Mr. Savisaar's party holds the capital of Tallinn in a profitable grip reminiscent of Tammany Hall. As soon as he was in charge at the Ministry of the Economy, Savisaar made it clear that he had it in for BRS.

Among other things, such as bad press directed at BRS, the Centre Party also used a state organ called the Railway Inspectorate as a tool to help keep Estonian Railways from attaining its goals. Not only was BRS tied up in red tape related to operating safety and other matters, but the Inspectorate began to compel Estonian Railways to allow Russian operators to compete on the basis of exceedingly favorable tariffs against BRS on BRS' own rail infrastructure. This was done by using European Union legislation that is designed to enable European firms to compete fairly. One of the instruments used to do this was the Estonian Railways Act of 2003. For at least a decade, Estonia has not had rail connections to Continental Europe. Currently, Estonia's rail network is essentially an appendix and terminus of the Russian system, used for transporting raw materials to the West, with the exception of a few passenger trains that serve the East, and some domestic passenger lines. Latvia and Lithuania maintain connections to Europe, but Estonia does not.

The topic of to whom Estonia is connected is especially relevant to this story: it is a tale of to whom you are beholden, both economically and politically. Since European rail operators cannot reach Estonia by rail, the EU legislation was used purely to benefit Russian railway firms. The legislation also served to drive out BRS and worked to the detriment of Estonia's security interests.

Seizing economic high ground?

Chou En-Lai said: "All diplomacy is a continuation of war by other means." The same also applies to cross-border business operations, particularly in contested areas, such as Estonia.

Russia tries vigorously to affect developments in the "near abroad" in Georgia, the Ukraine and elsewhere. While the US is overextended in other parts of the world and war-weary, and with the European Union concerned about energy dependency, much of the contesting in the "near abroad"—a phrase of Empire—gets done by the Kremlin. It would be naive to not regard the hounding out of Baltic Rail Services from Estonia in this context. Instead of Estonian Railways under the control of Western investors gaining access to Asian markets via Russia, as had been the aspiration of BRS, Russian petrodollars now penetrate ever deeper into Estonia and other contested markets, not just commercially, but politically. In earlier years, companies located in Estonia dealing directly or indirectly with the Eastern transit trade had a diverse ownership. Russian capital is now methodically buying up these Western and Estonian firms. Others are edged out.

Estonia's KAPO Security Police (an intelligence agency) has pointed to Russian money "seeping in" to Estonia as a security risk. Was Estonia safer with the national railway system in the hands of Western investors, than in the hands of Estonian politicians who are demonstrably vulnerable to the "eastern trade disease"? Is Estonia in jeopardy? I believe it is.

In April 2005, the KAPO detained Oleg Ossinovski, Chairman of the Board of the Spacecom rail firm, and accused him of trying to rig a cartel agreement with Estonian Railways. Spacecom is part of the large Russian Severstaltrans Group, specializing in freight transport. The former Director of Estonian Railways, Christopher Aadnesen, cooperated with prosecutors in their undercover investigation, but he has now returned to the US. It seems unlikely that the truth about what went down will ever be revealed in an Estonian court.

Initially invited to Estonia and then surprised to find themselves unwanted, the managers brought in by the BRS team battled vigorously for several years in an ever more hopeless situation, before finally throwing in the towel. On January 9, 2007, the government bought back BRS' 66% interest in Estonian Railways, ending over five years of private management of the rail sector. In a statement made in mid-January, Edward Burkhardt, one of the former owners of BRS, said in a television interview that the ruling Reform Party had asked for a one million euro bribe to facilitate the return of the railroad to state hands under terms favorable to BRS—an allegation that the Reform Party adamantly denies.

Large jingoistic ads on the front pages of newspapers now feature Centre Party candidates festooned with Estonian flags as the folks who “brought the railway back to Estonia.” Lest we forget, it was an Estonian government that initially invited BRS to carry out the privatization of the rail infrastructure. The subsequent Estonian government then did everything in its power, short of outright sabotage, to force BRS to quit the Estonian market. Estonia gave these Western businessmen a raw deal.

Ülo Matteus, who works as a counselor for the Press Service of the Estonian Parliament, expressed serious concern in a Delfi Internet portal feature on January 17 about the “money rules” mentality now running rampant among a great many Estonian politicians. Urmas Arumäe—a local official—suggested recently in an opinion piece that political parties ought to be financed from the state budget alone.

JaakValge, the scholar who researched the ill effects of the “eastern trade disease” of the 1920s, wrote a few years back in an article called “The Repulsive Attraction of the Russian Transit Trade” that it would be reckless for a significant part of the Estonian economy to be dependent on Eastern transit trade.

Edward Burkhardt directly criticized the Russian transport company Severstaltrans in the *Baltic Times* on January 24: “The biggest concern should be the control that Russian transport interests have over the Centre Party, and in turn over the coalition, and in turn over the government,” said Burkhardt, who feels that this is “an abomination for a free and democratic country.”

“Baltic Tiger” or “Socioholic”?

Ardo Hanson, a Harvard-educated macro-economist, helped to implement Estonia’s economic reforms in the early nineties. Back in those days, Hanson repeatedly warned against Estonia “falling off the wagon,” saying that the temptation to lapse into what he termed “socioholism” would be powerful. The renationalization of Estonian Railways appears to have made a prophet of Hanson.

Speaking recently to the *Eesti Ekspress* weekly, Henry Posner III—one of the former owners of BRS—said that after the adoption of the Railways Act in 2003, the state basically confiscated the majority of his company’s value. BRS reached the best agreement it could, considering the poor negotiation position it was in. Posner asserts that Estonia is getting back a railway system that functions a lot better than it did five years ago.

The Western investors didn’t do as well as they had hoped, but didn’t lose their shirts either, not by a long shot. If there are losers in this story, they are the Estonian people—through the erosion of Estonia’s international reputation and her security situation. Estonia’s vulnerability will increase even more should her growing economy slow, particularly if anyone that she owes money to should decide to begin to call in debts.

Edward Lucas, a seasoned Russia and Baltics hand, wrote recently in *The Economist* of the “suspicious renationalisation of Estonia’s railways [and] the rampant corruption in parts of government.” This is not how “tigers” behave; it is not the way of bold liberalizers. Edgar Savisaar hasn’t been able to carry out renationalization on the same scale that Vladimir Putin engages in, but the tendency is the same.

If Estonia continues to slip backwards, a new leeriness towards her will take root in the West, and Putin wins. Kadri Must—one of the rising young stars in the Centre Party—spewed venom at Ed Burkhardt in the *Foorum* television talk show on January 31. “How can he go around the world and leave the impression that Estonia is a small and grubby state?” fumed Ms. Must.

Ron Asmus, a veteran American analyst, wrote in the German weekly *Die Zeit* that “Russia is back—but not as the confident, democratic and pro-Western partner we had hoped for.” He describes Russia as an illiberal and increasingly authoritarian state. He notes that Russia, which views democracy on her borders as a threat, is assertively pursuing a policy of rollback against the orange and rose revolutions in such places as Georgia and the Ukraine.

I add that Estonia too has been the target of a variety of Russian active measures. Dr. Asmus writes that if the West is to help the cause of democracy within Russia herself, then “working for democracy on Europe’s periphery is critical,” and calls for the forging of a new “Transatlantic Ostpolitik”—one that combines competition and cooperation in regard to Russia.

If Ron Asmus senses a cold coming on in transatlantic relations with Russia, it is Central and Eastern Europe that may once again contract pneumonia. Estonia needs to lessen her addictive dependence on eastern transit trade, to diversify her sources of income and energy, to strive mightily against corruption in government, to restore her reputation, to speak to Western audiences with a persuasive message platform, and to lobby for the birth, as quickly as possible, of the new Transatlantic Ostpolitik that Ron Asmus envisions.

Estonia needn’t completely sever the blood vessels that connect her to Russia, but it would be in her interests—in view of Russian efforts to manipulate her neighbors—to become less dependent on that market, and to diversify. Russia is currently Estonia’s fourth trading partner behind Finland, Sweden and Germany. Above all, it is time to stop yakking about innovation and to do something. For a country that has always been nervous about security, working smarter would be one of the best ways to lessen Estonia’s security risks. [END]

Jüri Estam is a communications consultant who was born to Estonian refugee parents in Germany after World War II. Educated as a journalist in the United States, he returned to Europe in 1979, where he worked for Radio Free Europe in both the Estonian and English languages. He returned to Estonia during the week of the Moscow Putsch in 1991 and worked as a filmmaker and current affairs program host for Estonian Television.

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Does Ownership of Capital Matter?

The Growing Reach of Russian Money in Estonia

In addition to owning Spacecom, one of the rail transport companies that BRS had to contend against, the giant Russian steel company Severstal has also acquired the EOS oil terminal and owns several other oil terminals in Estonia. Journalist Peeter Raidla wrote in the business daily *Äripäev* in November 2004, after EOS was sold, that “Severstal has become the ruler of the Estonian fuel and transit business.”

Another Russian biggie in Estonia related to the energy and transit trade is the concern Russian Transgroup Invest, which owns a significant share of the recently constructed coal terminal at Muuga Harbor, with a capacity of five million tons of coal per year. This year, Nikolai Malohh Jr., the son of Nikolai Malohh, the Director General of the Russian Uralvagonzavod giant, a manufacturer of both transport and military equipment, succeeded in taking over an important railway carriage plant in Ahtme, Estonia.

The actual list of such greenfield investments, acquisitions and takeovers in Estonia by Russian capital is much longer. Virko Lepassalu — an investigative journalist who works at the Russian language newspaper *Vesti Dnja*, reported in a recent issue of *Saldo*, a business magazine, that the “Estonian economy looks more and more like a nut in a nutcracker, with Severstaltrans constituting one jaw of the nutcracker, and the machine producers in the Ural mountains forming the other jaw.”

It is not ruled out that the amount of American capital in Estonia may continue to decline, should Silver Point Capital Partners decide to sell Galvex, a metal galvanizing plant in Muuga Harbor, which is one of the largest of its kind in Europe. In the event Galvex is sold to non-Americans, the remainder of the firms based on American capital in Estonia would either be branches of such firms as McDonalds and Coca-Cola, or companies that are smaller, as a rule, than Galvex and the two American companies that held a stake in BRS.