

THE HISTORICAL  
ASPECTS AND CURRENT  
ISSUES  
OF THE DEVELOPMENT  
OF RUSSIAN-LITHUANIAN  
ECONOMIC RELATIONS

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*This article focuses on development of Russian-Lithuanian economic ties. The research and practical significance of this study lies in the identification of the sources of modern Russian-Lithuanian economic cooperation and the prospects of future mutually beneficial economic relations. The first attempt at establishing economic relations was made in 1919. However, young Lithuanian Republic gravitated towards the West, severing ties with the Russian market. However, the initiatives of Lithuanian authorities did not result in successful state building, and the economic situation remained unchanged. The USSR leadership made an effort to improve the living conditions in post-war Lithuania. There were some mistakes made in the relations with the local population that resulted in Lithuanians' resistance to sovietisation. However, in the conditions of post-war restoration of national economy and acute deficit of material and human resources, the Soviet leadership managed not only to reform and develop a socialistic economy in Lithuania but also to turn it into an industrial republic with developed agriculture and modern manufacturing facilities, whose major industries manufactured products used in nuclear and space technologies, aviation and navigation. The research shows that the post-Soviet period led to a dramatic change in Russian-Lithuanian economic relations; however, these relations retained potential for future development.*

**Key words:** Lithuania, Russia, economy, relations, market, crisis, agriculture, industry, prospects, development

Being neighbours, Russia and Lithuania are two countries that are destined to look for and take up any opportunity for multifaceted cooperation in the field of mutually beneficial interests.

Immediately after the termination of WWI, at the initial stage of development of both states, Russia used the political aspect in forging economic relations with Lithuania. So, as early as 1919, during the formation of the Lithuanian-Belorussian

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Soviet Socialist Republic, the government of the Russian Soviet Federative Socialist Republic provided it with financial assistance that amounted to 200m roubles. Despite their own problems, Soviet Russia and Soviet Ukraine supplied the new republic with raw materials, fuel, construction materials, foodstuff, etc. The Soviet Republic sent specialists in different fields to Lithuania; there was an attempt to re-evacuate the industrial equipment and other property transported during WWI. Customs barriers were lifted [1, c. 42].

However, the development of economic relations soon came to a standstill as a result of a number of circumstances (internal conflicts, internal ideological disputes, Polish occupation of Vilnius etc.).

In spring 1920, using a difficult political and military situation of Soviet Russia and its dire need for peaceful settlement of relations with the neighbouring countries, the Lithuanian party brought serious economic claims against Moscow.

Lithuania demanded that a part of Russia's gold reserve and its military and commercial fleet be allocated to the country. Also, Lithuania's claims included denationalisation of the property of Lithuanian citizens in the RSFSR; reparation of damage inflicted in the course of WWI; re-evacuation of property, capitals, deposits and railway vehicles that were transported from Lithuania in 1915 due to the German invasion; provision of weaponry and accoutrements for Lithuanian troops; allocation of a proportional share of Russian capitals and property abroad to Lithuania, and the purchase of Russian banknotes circulating in Lithuania [2, c. 711].

These demands put forward by Lithuania were not met. However, Vilnius was returned to Lithuania [see, for instance: 3, p. 10]. In fact, Russia did more than just returning the territory. Since Lithuania was plundered in the course of WWI and the Lithuanian people could not rapidly restore the economy on their own, the Soviet government decided to grant the Lithuanian government 3m roubles in gold without return. The Lithuanian historian K. Navickas, with a reference to Christian democratic periodicals, emphasises that Russia "helped Lithuania introduce its own currency in 1922 and thus commence the economic restoration of its territory" [4, c. 129—130]. However, in that period it was one of the last attempts of Soviet Russia to establish solely economic rather than political relations between the two countries. Nevertheless, it failed.

The pre-war economic development of the Lithuanian territory suggested activities within, first of all, the all-Russian market but after Russia's dismissal of the submitted economic compensation claims the Lithuanian government sought cooperation with the West.

It was not only severance from the Russian market; Lithuania also lost raw material resources. As a result, the industrial development policy formulated in the beginning of the 20<sup>th</sup> century (in Lithuania, it was aimed at catching up with more industrially developed future Latvia and Estonia) led Lithuania's economy to one-sided orientation towards agricultural production.

However, there were objective reasons behind such a situation.

Poland, having occupied the Vilnius region, isolated Lithuania from the USSR. The development of any relation with Poland was impossible for the

USSR. Lithuania agreed to establish diplomatic ties with Poland only in 1938, having recognised the loss of the Vilnius region [5, c. 36—38]. At the time, the economic interests of Lithuania were oriented towards the West.

Moreover, documents prove that by the beginning of WWII the Lithuanian economy was primarily agrarian and it lagged in terms of industrial development behind its Baltic neighbours [6, c. 460]. This fact can be easily explained. Before WWI, the structure of industry concentrated on the territory of future Lithuania was dominated by food processing and light industries (up to 70 % of the total industrial output), which is indicative of the agrarian type of economy [7, c. 11]. The orientation towards unilateral cooperation with the West did not give Lithuania any chances to catch up with Latvia and Estonia in terms of industrial development.

During the interbellum, a land reform aimed at creating a class of prosperous peasants was carried out in the country. This objective was to be achieved by means of establishing a single-homestead system. By 1938, single homesteads accounted for 84 % of all rural households [8, c. 50—51]. The concentration of lands in the possession of large proprietors in the zone of high-risk agriculture resulted in the fact that Lithuania's agriculture became predominately oriented towards livestock breeding. As a result of a narrow domestic market, the sale of livestock and flax cultivation products largely depended on western, especially German and English, markets. These countries accounted for from a half up to four fifths of Lithuania's export and import volumes, which allowed them to neglect Lithuanian trade interests and impose their will on the country. The dictates resulted in the fact that half of all Lithuanian farms sold livestock products abroad [9, c. 8].

Because of competition, Lithuanian trade partners did not aspire to develop industrial production of agricultural goods, being content with the export of agricultural raw materials from this country. Agricultural products accounted for 86—88 % of Lithuanian export [6, c. 472].

Overall, the land reform had a positive effect — the country's agriculture was developing: the amount of cultivated land grew up alongside increased crop yield, livestock number, and dairy and meat production. During the interbellum, livestock production increased by 23 % and reached 57.5 % of the gross agricultural output [8, c. 57; 10, c. 20—21].

At the same time, agriculture was developing rather slowly; the facilities, equipment and the quality of land were still at the pre-war level. Tillage and harvesting were not mechanised. Tractors and combines were not available, and horses were the only draught power. Rural areas were not electrified. Simple mechanical devices for grain threshing, cleaning and drying were used only at large farms. Excluding draught cattle, the total energy capacity of Lithuanian agriculture amounted to no more than 20—30 thousand hp [8, c. 58].

The described conditions of agricultural production resulted in rather low standards of living in the rural areas.

Apparently, Lithuania's sovereignty could facilitate the development of a number of manufacturing industries. In fact, some intensification did take place. However, the domestic market of manufactured consumer and industrial goods, equipment in particular, was quite limited due to low purchasing power of the population. With no support of a domestic market, Lithuanian

enterprises were not able to achieve a level that would allow them to sell their produce in other countries.

Thus, Lithuania's industry was developing rather slowly; such crucial for industrialisation branches as mechanical engineering and chemical industry hardly developed at all. The industrial structure was growing in a way similar to that of small agrarian countries. The food processing industry accounted for approximately 40 % of all industrial output, followed by textile and woodworking industries.

Before WWI, there were a number of Lithuanian large industrial enterprises, whose produce was sold in Russia. After the economic ties with the eastern neighbour had been severed, the produce of, for instance, large steel mills in Kaunas was in low demand. Plants reduced production volume and changed product ranges. The production of many types of goods became un-economic but it was profitable for producers as a result of high prices on the domestic market [8, c. 62].

Lithuania had large peat deposits; however, it was poorly exploited at an industrial scale. In 1938—1940, for example, 140—230 thousand tons were produced annually, which accounted for less than 0.1 % of the proven peat deposits. In the fuel balance of all industries (including energy production), it accounted for mere 8 %. Hydropower resources were hardly exploited either. The existing combined cycle power plants used imported coal and diesel fuel. Approximately 300 thousand tons of coal was imported annually; a significant part of this amount could have been replaced by local fuel. Power consumption was rather low, which was indicative of a low technological level at most industrial enterprise in Lithuania [11, c. 3].

In August 1940, Lithuania became not only the 13<sup>th</sup> republic of the USSR but also a site for establishing a new economic order. The republic could count on the economic support of the whole country. In effect, in 1940 Lithuania attempted to make a breakthrough in economic (as well as social and cultural) development.

On its own, an agrarian country with backward agriculture, and a low level of mechanisation and education could not achieve such a breakthrough.

At the same time, the command and control system developed in the republic on the basis of significant Soviet resources could not only ensure continuous operation of the nationalised industry but also intensify it by as early as summer 1940.

During the interbellum, a narrow domestic market and limited export opportunities presented a formidable obstacle to the development of Lithuania. After the economy of the Republic of Lithuania had been integrated into that of the USSR, the problem of a sale market was eliminated and the internal demand for manufactured goods increased considerably.

Consequently, there arose a need to extend the range of industrial products, especially consumer goods. The 1941 plan anticipated a 2.5 fold increase in the nationalised local industry's output; the main objective of the plan was to meet local needs by means of local production [12, l. 3].

According to Lithuanian economists, in 1941 the investment in the economy of Soviet Lithuania was meant to increase by 234 % in comparison to the record investment registered in bourgeois Lithuania in 1939. A compre-

hensive capital development plan was devised. In 1941, industrial production increased by 75 % compared to 1940 [13, c. 16].

According to Lithuanian experts, the tasks set in the 1941 industrial production plan and scheduled for the first half of 1941 were successfully completed earlier than expected — with the help of other republics of the Soviet Union who shared their industrial practices with Lithuania and met its sharply increasing demand for materials and means of production (equipment, metal, coal, oil, chemicals, cotton, etc.) [14, c. 7].

The plans for accelerated economic development of the Lithuanian SSR were disrupted by the German offensive against the Soviet Union.

The restoration of Lithuania's economy started immediately after its territories had been liberated from German occupation. In the conditions of considerable uncertainty, the first budget was drawn up for the remaining months of 1944. In October 1944, it was adopted as "The state budget of the Lithuanian SSR for 1944 and the 4<sup>th</sup> quarter of 1944" nmbly a decree of the Council of People's Commissars of the USSR [15, l. 9].

It is worth noting that the subsidies from the Soviet Union's budget accounted for two thirds of the Lithuanian Republic's budget (220 mln 179 thousand roubles and 140 mln 210 thousand roubles respectively). Paragraph 3 of a decree issued by the People's Commissariat for Finance stipulated that in the 4<sup>th</sup> quarter of 1944 a sum of 63.4m roubles should be allocated to the Council of People's Commissars of the Lithuanian SSR from the reserve fund of the Council of People's Commissars of the USSR to cover expenditures against the budget of the Lithuanian SSR [ibid].

From July 1944 until the end of the year, a lot was done to restore the shattered economy and create normal living and working conditions. As a result, 435 industrial objects came into operation over a year; power plants of a total capacity of 7000 kW were partially or completely restored in 20 cities. A total of 89.5 thousand sq m of residential accommodation was newly built [16, l. 7].

A similar situation regarding the fulfilment of the economic plan was observed in 1945. The pace of works was accelerating; more and more objects were being put into operation.

Economists emphasise that a rapid growth in Lithuania's economy began in the 1950s. This success depended on the development of heavy industry and, first of all, mechanical engineering. At the same time, special attention was paid to knowledge-intensive production (radio electronics, instrument industry and machine tool building, electrical engineering, etc.) [17, c. 111, 142].

A high rate of industrial development of Lithuania over the next years contributed to deeper integration of its economy into that of the USSR's. The economic integration was a two-way process: the republic opened its economy to the needs of the big country, receiving in return massive support of the whole Soviet Union, which exceeded the opportunities of the Lithuanian SSR manifold in the course of early development of the republic's economy. In particular, in the state budget of the Lithuanian SSR for the 4<sup>th</sup> quarter of 1944, the Soviet Union's subsidies accounted for two thirds of the republic's budget. Even later, at least until the mid-1950s, the republic was receiving allowances from the central budget (internal income accounted for less than 20 % of the budget profit) [15, l. 9].

The integration process was facilitated by the establishment of a unified republican energy system and a pipeline network in the 1960s. The Dashava-Minsk-Vilnius gas pipeline (1961) and the Polotsk-Mažeikiai oil pipeline (1979) contributed to the development of chemical industry in Lithuania (a chemical plant in Kėdainiai, oil refinery in Mažeikiai, etc.) [18, c. 17].

The republican strategy for energy development was thoroughly revised. Lithuania's leadership supported the idea of creating an isolated energy system in the Lithuanian SSR. The strategy envisaged construction of small, often unprofitable, combined cycle and hydro power plants using local energy resources and imported fuel. The largest capacity was meant to be concentrated in the Kaunas system covering a considerable part of the republic's territory [19, l. 4, 7—8].

By the mid-1950s, the total capacity of electricity generating plants in the republic amounted to 188.2 thousand kW. In 1955, the construction of the Kaunas hydroelectric power plant of a capacity of 90 thousand kW was commenced. Similar to the first post-war years, almost the whole Soviet Union was involved in the construction of this object. Gorky, Minsk, Narva, Kostroma, Kuibyshev and other cities provided the construction site with equipment, materials and qualified staff [20, c. 114—115].

In 1960, the Kaunas HPP was put into operation. However, this success was the last achievement of the advocates of hydroelectricity development and the independent energy supply system on the republic's territory. A rapid industrial growth and the planned full electrification of agriculture required a sharp increase in power production. In 1958, Lithuania produced four times as little power as the national average [21, c. 11].

The Kaunas HPP did not ensure the alignment of energy development. On the contrary, it became evident that the construction of new hydropower plants was a dead end in the development terms. The orientation towards an independent isolated republican energy system did not justify itself.

In the early 1960s, the solution to Lithuanian energy problem was approached by the centre: the construction of hydropower plants was suspended and the construction of the Elektrėnai power plant of a capacity of 1.2m kW was commenced. It was just the first stage of the energy integration of Lithuania into the large energy sector of the USSR. In the 1970s, the Soviet leadership came to a decision to construct a nuclear power plant in Lithuania [22].

A specific feature of the economic development of Lithuania in the 20<sup>th</sup> century was an industrial leap that took place in the Soviet period. In view of the current negative attitude to that period in the former Soviet republics, it is worth noting that it was Lithuania where industrial development unfolded according to well-devised and clear plans. These plans ensured both the development of knowledge intensive production (electrical and radio engineering, precision instrument industry, etc.), which enabled Lithuania to reach the industrial level of its neighbours, and the development agriculture.

Experts estimate that Lithuania witnessed an increase in national income per capita that was the most rapid in the country in the late 1980s: in 1985—1989, it grew by 22.2 %, whereas the national average was 7.1 % [23, c. 13]. Moreover, Lithuania performed well not only in terms of the generated but

also used national income. With a few exceptions, the use exceeded the income generated. In 1988, this difference amounted to approximately 10 % [24, c. 88].

The difference in national income generation and its use was created through economic ties at the expense of other republics. In the course of the Soviet Union integration, the intensity of economic ties was increasing. At the same time, over the last two decades, import exceeded export. One should not forget that the principal raw material for Lithuanian industries was the produce of other republics' extractive industries, which was supplied at evidently lowered prices. So, in 1989, oil, coal and gas were sold in the country at prices 2—2.5 times as little as the world average [25, c. 5]. Consequently, the generated national income of the Lithuanian SSR stemmed from appropriating a part of the national income of other Soviet republics. Thus, intra-union economic ties can be called one of the means of resource redistribution to the benefit of the Lithuanian SSR.

In general, the history of development of the Baltic region states in the 20<sup>th</sup> century makes it possible to speak of pronounced contradictory trends of integration and isolation as well as changing socioeconomic development and cooperation vectors.

In effect, Lithuania always had a choice between active interaction with the all-Russian market and abrupt severance of external economic ties.

In the 20<sup>th</sup> century, Lithuania made two attempts to enter the European market. The first attempt (1920—1930s) did not succeed. The initiatives of the then authorities resulted in territorial problems, the backward economic condition of the country, persistence of traditional agrarian production, a low level of technical equipment and a low standard of living of the majority of population. As to the economic performance, Lithuania lagged behind even its neighbours — Latvia and Estonia.

Over the next two decades, despite the damage inflicted by WWII and the loss of state sovereignty, backward agrarian Lithuania returned to the Russian market and turned into an industrial-agrarian republic with developed agriculture and cutting-edge industry, whose key branches manufactured products used in nuclear and space technologies, aviation and navigation.

The second “westernization” attempt made in the end of the 20<sup>th</sup> century was a result of both the abrupt severance of economic ties with Russia and other former Soviet republics, and the fundamental restructuring of economy towards its simplification accompanied by material and social losses. The Russian-Lithuanian market almost ceased to be. Ties between enterprises were cut; borders were closed for both agricultural produce and other goods. One had to start from scratch again. At the same time, the Lithuania-Russian economic ties developed according to strict market principles.

The origins of modern economic relations between the two states are to be sought in the agreements concluded during the first years of the newly established Russian Federation and the Republic of Lithuania. The foundations of trade and economic cooperation between Russia and Lithuania lie in the 1993 agreement, which was revised in 2004 when the Russia-EU partnership agreement came into force for Lithuania [26].

Since Lithuania's “turn to the West”, the principal problems of bilateral economic relations have been trade and transit. Both problems are related to

ensuring the day-to-day functioning and development of the Kaliningrad region of the Russian Federation, a Russian semi-enclave in the European Union.

Measures towards establishing working relations in the field of economy proved to be short-lived and unreliable largely due to political complications. Some stabilisation was observed after Lithuania's accession to the EU as several intergovernmental disputes have been settled with the EU's participation.

Later, despite the persistent difficulties in political relations between the two countries, the Russian-Lithuanian trade and economic cooperation started to improve. In 2006—2008, the volume of bilateral trade achieved \$5 bln. The 2008 crisis slowed down this process — in 2009, the volume of bilateral trade decreased to \$4.2 bln. However, 2011 saw a rapid growth: the volume of bilateral trade increased by 87.3 % from 2010 (\$4511.9m) and achieved \$8437m. In the first quarter of 2012, the volume of bilateral trade also increased [27].

The development of investment activity remains contradictory. In particular, there was a decrease in investment activity in 2010—2011, which can be viewed as a reaction of Lithuania's economy to the 2008—2009 crisis.

However, one can expect some intensification in the Russian-Lithuanian economic relations. Lithuanian products are facing fierce competition in the West, whereas there is traditionally high demand for them in Russia.

It is worth noting that large Lithuanian investment projects are implemented, as a rule, in the Kaliningrad region, for example, the fish processing enterprise Vichiunai-RUS (\$7m), the meat processing company Kaliningradsky delikates (\$7m), the Akropol shopping mall (\$18m), etc. Moreover, in autumn 2012 the Lithuanian company ARVI ir Ko signed an agreement with the government of the Kaliningrad region on the construction of a sugar mill in the Slavsk district. The project's budget is estimated at 5 bln roubles [28, c. 15].

The Russian-Lithuanian economic cooperation in the 20<sup>th</sup>-21<sup>st</sup> centuries has experienced its ups and downs. However, despite historical and political disturbances, both countries — either quickly or over long intervals — always found opportunities for establishing mutually beneficial contacts. The bilateral relations have not been limited to trade and solving transition or other local problems; the range of links has become rather extensive.

Today there emerge new opportunities for economic cooperation between the two countries in view of Russia's accession to the WTO, an increasing role of cross-border and trans-border cooperation, and the innovative development of the regional (Baltic) economy. Alongside bilateral Lithuanian-Russian relations in the field of economy, one should not overlook the geographical and political features of the two countries as members of large unions (the EU, EurAsEc, etc.) as the process of building inter-union relations can require the countries' cooperation experience.

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