BE AFRAID OF YOUR DREAMS, THEY MAY COME TRUE!

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The month of November 2016 in Cyprus was marked by the collapse of another round of negotiation efforts by the two communities to find the right formula for co-existence on the island. The unfortunate result was followed by the flood of commentaries and debates among local politicians and experts. To sum up, the dominant narrative in the public space was the following: bitter sorrow of the lost opportunities, eternal peace and economic bonanza, which were supposed to come with the agreement, and a concern about uncertainty stemming from the deadlock and lack of alternative negotiating scenarios.

Suddenly, presumably after massive pressure from foreign centers of power, early December has brought life back into something, which was considered terminally dead several days earlier, with leaders on both sides of the divide declaring full commitment to continue negotiations that may lead to unification of the island on the basis of a loose federation sometime next year.

While hectic negotiation process with U-turns is still under way, it is important to take one more time a closer look at the model, which is called by its local architects and many foreign supporters "the last chance of the Cypriot people".

The model on the offer is called "bi-zonal federation" made of two equal constituent states and a federal government with limited authority and rotating presidency. While many supporters and opponents, mainly, debate about the "equal" element (given that one community is much smaller than the other), it is the "state" element, which requires special attention, since it is this very nuance, which introduces internationally-recognized legal framework for the creation of two separate nation-states (with all the relevant attributes) sharing one small island, which then come to form a federation of equals.

The main argument of the architects is that there is no other option for unification. And while downplaying anything related to the risk stemming from the "state" element, the model is marketed under the premise that a solution would unlock unutilized hidden economic potential of the island, lead to economic synergy spurred by increased security and political harmony. The main drivers of a future economic boom are envisaged to be energy, tourism, international education, construction and international finance, which would attract massive investments, mainly from overseas, which in turn would help cover the costs of unification.

There is no doubt that the pursuit of a solution is a worthy cause, and no one can deny the Cypriot people the right to define the destiny of their land, and to heel the historical traumas of 1974. Being strong nationalists (which is not a bad thing altogether), they mainly do not like resident foreigners commenting on their domestic issues, especially, the Cyprob.

The reason behind my decision to join the chorus of many local commentators is one small irony – the economic boom promised under the proposed solution model will heavily depend on how successfully it will be marketed to foreign investors, foreign resident businessmen, foreign tourists and foreign students. The sad truth is that after a decade as an expat consultant on the island and the region, I do not observe shared optimism in the foreign expat business community about the model on the offer – the dominant sentiment varies between very cautious wait-and-see and outright rejection.

The main explanation is …. *complete uncertainty* and perceived high risk of a possible fall-out, and further military confrontation between the two proposed constituent states during the implementation phase.

The uncertainty factor is composed of multilayer issues: timing of unification, escalating global and regional geopolitical, economic and financial turbulences, legal and regulatory ambiguity, transitional operational havoc related to harmonization of political, legal and financial systems, lack of local and international expertise on practical implementation of unification process. These factors are magnifying the risk of a fall-out between the two communities, which practically never lived together, speaking different languages, having different religions, and in many ways, mentality.

It is under these objective circumstances foreign investors will be offered to bring money to Cyprus to spur the promised economic boom.

Truth to be said, the world has accumulated enormous collective experience in dissolution or outright destruction of states, and almost no experience on how to unify them, and even when unification was happening, it was mainly achieved with iron and fire. The closest available successful and peaceful experience to look at was that of Germany almost thirty years ago.

However, a closer analysis of the German case, ironically, emphasizes everything what the proposed local model is not, which only amplifies the reservations foreign businessmen in Cyprus have about current unification structure.

Despite the fact that it is politely called unification, in reality, it was absorption of Eastern Germany by the Western part, where former communist territories came under control of a strong national administration in Bonn with West German laws and regulations methodically imposed on the new lands and people, who spoke the same language, belonged to the same ethnicity and faith, and mainly shared deeply-rooted German national character, common history and culture.

In contrast in Cyprus, a unification is proposed with the purpose of de-facto subsequent devolution, where a newly-introduced federal authority with limited powers will co-exist alongside separate constituent states, each governing its own territory. How legal and regulatory issues will be finetuned in practice in such a tripartite construct is yet very much unclear.

By the time of unification West Germany was practically the strongest and the fastest growing economy in Europe with enormous accumulated wealth and administrative prowess. As for the Eastern Germany, no matter what they say in the West of the country, it was an accomplished state in its own name with a strong army, highly educated population and rich technological and scientific potential, which contributed substantially to future success of united Germany. However, even with all that available economic wealth, it is openly admitted today that the cost of unification will never be recovered by Germany – so expensive it was.

In Cyprus, having lived through economic destruction of 2013, overburdened with debts and ailing financial system, the Republic of Cyprus is planning to unite with a subsidized entity striving to come out of a decades-long isolation and gain recognition beyond the only foreign state, which is simultaneously its main economic and security donor.

German unification had very high economic, psychological and human cost, and despite all the strengths, the harmonization of the two parts in many ways continues till today. But Germany escaped much of the pain and costs thanks to one more factor of critical importance, which many tend to overlook – it is timing. The unification happened when the collective West won the so called Cold War, when dissolution of the USSR eliminated the main geopolitical danger, and overwhelming peace set upon Europe and the Western world. The period of 1990s became the golden era of unprecedented economic growth, expansion to new markets and enormous profits. The tide which was going up took united Germany with it and helped to compensate for the losses and minimize pain.

Unfortunately, the Cypriots approached possible unification at the time when the golden era of prosperity has finished, and the world has entered the period of a long-term economic and geopolitical crises with growing destabilization to come. In contrast to Germany, which profited from European peace and prosperity of 1990s, Cyprus is part of broader Middle East, the region of growing chaos and militarization.

Expectation of massive investment inflows in case of unification is a dangerous proposition at the time when Cyprus' main trading and investment partners entered economic crisis, and the nature of the main local industries will be changing dramatically in the near future under the pressure of global trends. Russia is suffering from low oil prices, Western sanctions, military costs and lack of domestic structural economic reforms, which directly affect the profitability of its companies and purchasing power of its population that will not be travelling abroad in the future as it used to in the past, and Russian businesses no longer use Cypriot financial system as before. Britain, having voted for Brexit, will be in the state of economic turbulence and uncertainty for years to come with the falling pound cutting on the budgets of British holiday makers. The Eurozone is in crisis with major banking and financial turbulences still looming. Growing euroscepticism amplified by the economic woes, puts the whole EU project in front of existential challenge of unprecedented scale. Turkey, as the main donor of the Turkish Cypriots, although a dynamic economy but still remains in the category of emerging markets and is overly dependent on its construction sector, and thus, highly susceptible to interest rate fluctuations in the US and sales to the rich world. There is high probability that the US Federal Reserve will start raising interest rates next year, which will provoke crisis in the emerging market economies and capital outflows. Turkey will not be the exception with Turkish lira already losing up to 20% this year alone, and nothing promises the situation will improve.

The problem of the world today is that the global economy has not recovered from the crisis of 2008. None of the underlying issues has been resolved: falling productivity, growing debts and narrowing room for monetary policy maneuvering continue increasing pressure on falling global demand, investment returns, growing poverty and ever slowing global economic activity with all the relevant negative consequences for every country on the planet.

In such a global and regional environment, which investors are going to commit their money to a newly-born state with a fragile political structure and unclear regulatory framework?

One would obviously argue that there is a hidden ace - the offshore gas sales. First of all, it is widely known that the oil and gas market is living by fourteen-year price fluctuating cycles. The period of high prices has ended two years ago, and the market is now in the new downward phase, which directly affects the economic viability of any project. Second, local public debate often presents future gas revenues as readily available funds immediately after the signing of unification agreement. It is not an industry secret that the fastest projects of such nature take no less than seven years to start rolling. Others, especially those involving complex geopolitical considerations to overcome, may take up to twenty years before coming on stream, and no guarantees attached.

Third, there are several misconceptions widely circulating in Cyprus about direct correlation between geopolitics and energy, and about trade and mutual investments strengthening peace and cooperation between countries.

It is well known in the academic world that the link between energy and geopolitics has very weak historical evidence. Even in the heat of the Cold War, the USSR never stopped sending gas to the West. And late president Chavez, while passionately condemning American imperialism, was diligently sending oil tankers to the US. At the same time, flourishing trade and mutual investments did not prevent European powers to ruin each other to the ground one hundred years ago. And the list of evidences goes on.

These few examples are to counter the false argument that unification in Cyprus will open the door to joint exploitation of energy reserves in the East Mediterranean, which in turn will create such economic integration (involving Turkey) that will eliminate the risk of war between regional players because mutual economic benefits will outweigh military and other geopolitical considerations. This is a dangerous illusion to be entertained with. It is equally dangerous to think that a hypothetical gas pipeline to Turkey (which is recognized by the industry experts as the only economically viable option under current market conditions) will give Cyprus any leverage over its northern neighbor. Turkey, a big economy with growing population, has multiple diversified energy sources. And even if the Eastmed gas starts flowing North, its overall share in the Turkish energy mix will not exceed an estimated few percentage points, which represents no leverage at all. At the same time, there is a plausible risk that gas revenues coming from Turkey will create disproportionate dependence of Cyprus state budget on the sales to its neighbor.

It is important to emphasize that the purpose of this text is not to discourage unification. On the contrary, I would strongly argue that unification of Cyprus is a worthy and honorable cause to pursue!

The purpose of this argument is to share legitimate and reasonable concerns of foreign business community (whose contribution to the economic success of unification is expected to be considerable) that in the eyes of many among them the model on the offer is de-facto "devolution through unification", and it contains many architectural flaws and false calculations with long-term existential consequences for the island.

It is the choice of the Cypriot people and theirs only, but at the time of historical shifts in the global and regional geopolitical geometry, it is also wise to practice prudence, and assess risks behind promises of eternal prosperity and peace. And never forget that the RIGHT TIMING is half of success.

Colin Gray, one of the world's renowned scholars of war, writes in one of his forty maxims on war, peace, and strategy: "Prudence is the supreme virtue in statecraft and strategy. ….. The prudent strategist is alarmed by a policymaker who is so fixated upon desirable goals and their anticipated benefits that risks are not properly assessed".[1]

[1] Colin S. Gray *Fighting Talk: forty maxims on war, peace, and strategy* Potomac Books, p. 131.