

April 2010

Rough First Draft

Not for Quotation

per.wijkman@telia.com

**The Eastern Partnership Countries in Transition:
Just Good Neighbours or one of the Family**

Per Magnus Wijkman

Table of Contents

1. Introduction
2. A Reminder of Basics
 - 2.1 The Renewed Importance of Openness
 - 2.2 The Increased Importance of EU Absorption Capacity
3. Free trade as a Means to Further Peaceful Relations
 - 3.1 Results of the Barcelona Process to date
 - 3.2 Results of the Eastern Partnership to date
 - 3.3 The Prospects for Success
4. The Importance of Soft Power
 - 4.1 The Prospect of Accession
 - 4.2 The Importance of Institutions
5. The Importance of Hard Power
 - 5.1 The resolution of regional conflicts
 - 5.2 The Need for new institutions
 - 5.3 The Need for Donor Co-operation
- 6 Conclusion

1. Introduction

Richard Baldwin concludes his pioneering work *Towards an Integrated Europe* by quoting Jacques Delors' statement in January 1994 that "Europe needs to know where it is going". He adds that a more appropriate comment might have been that "Europe needs to know how to get [to] where it is going and what to do in the meantime." (p.223). Baldwin's comment remains relevant today as the EU continues to define how to get to where it wants to go, how long it will take to get there, and what to do in the meantime.

The EU has gone far. Since Delors' statement in 1994, 15 States have acceded to it (in 1995, 2004 and 2007). But the further it goes the more questions it faces. More countries want preferential access to its market, the larger that market becomes. More are attracted by its core principles the more successfully the EU applies them - preservation of peace, defense of democracy and human rights, strengthening of market economies. This creates a dynamics of mutual interaction, where the EU attracts its new neighbours and in turn is attracted by its own self-interest to resolve conflicts in its immediate neighbourhood.

Small wonder then that the EU over the past decades has increasingly struggled with the question of how to treat its neighbours – both as an issue of foreign and security policy and of enlargement. To develop a consistent policy under ever-changing conditions is to shoot at many moving targets, a difficult and risky process. The Barcelona Process during the Spanish Presidency (Spring 1995) aimed to involve the countries of the Southern Mediterranean coast. Leading up to the big bang enlargement of 2004, the Commission aimed to stave off new membership applications and was prepared to offer "anything but membership" in the famous words of Romano Prodi (2002). The result was the Commission's proposal in 2004 for a European Neighbourhood Policy (ENP). Enlargement Commissioner Günther Verheugen had noted in 2003 that this policy was to concern countries for which accession was "not on the agenda". Already a year later Verheugen had modified, if not clarified, his position by stating that the ENP "neither prepares for enlargement nor rules it out at some future point" for participating countries. The ENP was less relevant for the countries of the Western Balkans since the European Council in its Thessaloniki Declaration of June 2003 had stated that "the future of the Western Balkans lies in the European Union."

The neighbourhood policy includes ten States on the Southern and Eastern coasts of the Mediterranean¹ and six States in Eastern Europe and the Southern Caucasus². In order to invigorate the Barcelona Process, the French Presidency (Autumn 2008) proposed the Union for the Mediterranean. Almost immediately, Poland and Sweden proposed the Eastern Partnership which was adopted by the Council during the Czech Presidency (Spring 2009). This "emphasized the need for a differentiated approach respecting the character of the ENP as a single and coherent policy framework." (Com(2008) 823 final, p. 2) - no easy task!

In summary, the countries bordering the EC fall into the following groups.

¹ Algeria, Egypt, Israel, Jordan, Lebanon, Libya, Morocco, Palestinian Authority, Syria and Tunisia plus four coastal states in the Western Balkans that are potential EU candidates along with Turkey.

² Belarus, Moldova, Ukraine and Armenia, Azerbaijan, Georgia respectively.

1. Acknowledged candidates for full membership. The EU is conducting accession negotiations with Croatia and Turkey and is considering Macedonia's application. Croatia is likely to accede in the next few years while the time-table – and indeed the outcome- for Turkey and Macedonia is less certain.
2. Acknowledged potential candidates. The Thessaloniki Declaration of 2003 states that the “future of the countries of the Western Balkans lies in the European Union.” Most recently Montenegro (2008), Albania (2009) and Serbia (2009) have submitted applications for membership. Accession negotiations with all these potential candidates are likely to take several years to start.
3. Unacknowledged potential candidates. The six countries of the Eastern Partnership could be candidates if deemed to be European nations in accordance with Article 49 of the Treaty of the EU. This is most likely the case for the three countries of Eastern Europe (Belarus, Moldova, Ukraine) and possibly also for the three countries in the Southern Caucasus (Armenia, Azerbaijan, Georgia), which border Turkey, a possible future EU member. Georgia, Moldova and Ukraine have expressed interest in membership.
4. Non-candidates. None of the southern Mediterranean coastal States qualify for accession in accordance with Article 49 of the TEU. This Article disqualified Morocco's application for membership in 1987, an important precedent. Several EU Member States (UK, France, Spain, Italy) have strong ties to and interests in several of the Southern Mediterranean coastal States. These countries tend to drive the Barcelona Process.

Russia requested to have its own Strategic Partnership with the EU and is not a member of the ENP. While not institutionally present, it casts a long shadow in conflicts that plague the Eastern Partnership (Transnistria, Abkhazia, South Ossetia, Nagorno-Karabakh).

The EU's first priority is to negotiate accession with Turkey and the countries in the Western Balkans. This will take at least a decade. Thereafter, the EU will be in a position to consider the membership prospects of the Eastern Partnership countries. This is likely to take another decade. Two decades is a long 'meantime'. During it, the EU must devote significant resources to managing the Eastern Partnership within “a single and coherent policy framework” where one size will not fit all. Simultaneously, it must develop and apply farsighted policies vis-à-vis the countries of the Southern Mediterranean. This paper illustrates some factors that are important for making these differentiated policies a success.

2. A Reminder of Basics

Before dealing with these issues, it is useful to recall two recent and interrelated changes in the European Union. Firstly, in its transformation into the European Union, the European Community became less of an exclusive club and one more open to enlargement. Secondly, and partly as a result, the capacity of the EU to absorb new members became an increasingly important determinant of the speed of enlargement. This section recalls these two background issues.

2.1 The Renewed Importance of Openness

“Nous ne saurons jamais trop redire que les six pays qui forment la Communauté sont les pionniers d'une Europe plus large dont les limites

ne sont fixées que par ceux qui ne s’y sont pas encore joints.” Jean Monnet, Mémoires, s. 576

‘Outside observers’ in the 1960ies and 1970ies saw the European Community as an exclusive club, a closed shop. An iron curtain separated Western and Eastern Europe. Western Europe itself was at sixes (EC) and sevens (EFTA). Shared sovereignty was a key element in the former. The latter was primarily a free trade area. In the vision of Jean Monnet, shared sovereignty was what could convert economic integration into a political peace process. Given the historical importance of ensuring peace in Europe after two world wars had started there, he envisaged a Community open to membership for all interested European countries. But while the post-war Committee for European Economic Cooperation was open for all, the USSR prevented the countries of Eastern Europe from participating and the ensuing cold war caused neutral border states to abstain. The UK, still a residual global power, shunned the supranational elements in the coal and steel community and the proposed European Defense Union. Dictatorships in Southern Europe disqualified some countries there. Thus, the European Community became primarily a French-German peace project, cheered on by the small Benelux countries – the historical invasion route of armies - and joined by the Italians eager to forget Mussolini.

As the Commonwealth faded in importance, the UK reconsidered and overcame French resistance to join in 1973 – bringing Ireland and Denmark with it. The fall of dictators in Southern Europe enabled Greece to join in 1981 and Spain and Portugal in 1986. However, it was the fall of the Berlin Wall in 1989 that changed everything. This, and the consequent dissolution of the USSR in 1991, allowed three neutrals (Austria, Finland and Sweden) to join the EU in 1995. The consolidation of most of Western Europe into the EU naturally led the countries of Central and Eastern Europe including the re-independent Baltic States to ask for accession negotiations. As a result Monnet’s peace process was extended from Germany’s western to its eastern neighbours: Czechoslovakia, the victim of the Munich Agreement, and Poland and the Baltic States, victims of the Ribbentrop-Molotov pact.

This fundamentally transformed the nature of the European Union, imparting a tremendous political dynamic, which is now reshaping Europe. An exclusive club in the sixties and seventies, the EU is now committed to post-war reconciliation and reconstruction on a Pan- European scale. Also those countries in Eastern Europe that wish to join can do so provided they fulfill strict preconditions. Enlargement is now driven by conditional self-selection and constrained by the capacity of the EU to absorb new members.

2.1 The Increased Importance of EU Absorption Capacity

With many applicants for accession, the absorption capacity of the EU becomes an important constraint on its enlargement. The EU requires time to absorb recent members, to implement its new constitution and to reconcile differing internal opinions concerning further enlargement. The most recent Eastern enlargement has illustrated the risk that premature accession can compromise core values of the Union and has created second thoughts about accepting new members. Internal politics and decision-making processes become increasingly complex and cumbersome the greater the number of members in the Union. The requirement of unanimity, and in some cases national referenda, makes accession akin to entering the eye of a needle. Summarized in the expression ‘enlargement fatigue’, these various factors contribute in differing degrees to complicating and slowing down enlargement.

3. Free Trade as a means to further peaceful relations

“The natural effect of trade is to bring about peace.” Montesquieu (1758)

Free trade and the common institutions necessary to govern it contributed importantly, in Monnet’s view, to promoting post-war reconciliation and maintaining peaceful relations between former belligerents. This is a basic tenant of the European Community and it is hardly surprising therefore that the Commission should propose it as a key element in the ENP. The backbone of the ENP is the offer to neighbouring countries to negotiate free trade agreements of two kinds: traditional, shallow agreements for industrial goods or deep and comprehensive free trade agreements (DCFTAs) encompassing goods and services and various trade related regulations. These agreements can be bilateral with the EU and furthermore between the neighbouring countries themselves. DCFTAs are ambitious and complex, requiring partners to harmonise much of their trade-related legislation on that of the EU. The countries must agree *inter alia* to:

- establish competition laws and procedures (including public procurement) based on the EU *acquis*, including establishing an independent competition authority.
- adopt international and EU laws and procedures concerning sanitary and phytosanitary measures and have an institutional capacity to apply them. It must do the same concerning technical barriers to trade.
- adopt and apply WTO rules concerning intellectual property rights.
- take on board major parts of the EU’s trade related *acquis*, such as preferential rules of origin, services and foreign investments.

To accomplish this is a major challenge for any newly independent nation that lacks national institutions and has only recently started the transition to a market economy. But the pay-off is great because DCFTAs give access to the EU’s internal market. The DCFTAs also provide a crash course in accelerating transition to a market economy, thereby increasing economic growth. What has the reaction of the ENP countries been to this offer? What are the prospects for success?

3.1 Results of The Barcelona Process to date

The Barcelona Process established in 1995 set as targets for each neighbour country to conclude a bilateral free trade agreement with the EU as well as free trade agreements with each other before the end of 2010. Achieving both these targets would create a single market encompassing all the EU and Southern Mediterranean States.

The EU has concluded bilateral agreements with all countries but Libya, which is in progress but not yet operational (?). Most of these are ‘shallow’ agreements (those with Egypt, Israel, Jordan, Morocco and Tunisia being exceptions). Free trade has also been achieved between all Arab countries on the Mediterranean coast through the agreement on the Pan-Arab Free Trade Area (PAFTA) established at the initiative of the Economic and Social Committee of the Arab League in 1997. PAFTA realized free trade in industrial and agricultural goods in 2005. It is a shallow free trade agreement (not dealing with services and other trade related issues?). It includes eight Arab League countries which are not members of the Barcelona Process.

Four countries (Egypt, Jordan, Morocco, Tunisia) signed the Agadir Declaration in 2002 and thereafter negotiated the Agadir Agreement which entered into force in 2004. This established free trade between them in 2005, five years ahead of schedule. This Agreement is deeper than PAFTA, providing *inter alia* for diagonal cumulation of origin through adoption of Euro-Med protocol on rules of origin. While trade between the four Agadir countries is modest, it is greater than in PAFTA and constitutes about a fifth of their total trade, in spite of the fact that the four countries are not contiguous to each. Intra-Agadir trade is likely to grow as products containing inputs from any of the four countries qualify for tariff-free entry to the EU. PAFTA countries take a negligible part of EU foreign direct investment. Diagonal cumulation of origin is essential to attract such investments as the production processes unbundles and factories import inputs from partner countries and export the assembled final product to the EU.

In a mistaken interpretation of cause and effect, the modest level of intra-regional trade in the Southern Mediterranean as a whole may have contributed to keeping most of the regional trade agreements shallow.³ However, as other countries deepen their trade agreements with the EU, the PAFTA countries will have an increased incentive to deepen also their own trade agreements – as the Agadir countries have done – and in particular to adopt Euro-Med rules of origin. Gravity type studies that show a large unrealized potential for regional trade could also encourage deepening these agreements.

More than a decade's track record shows that progress has been made by avoiding the most difficult – and also the most important – issues. The depth and the scope of these trade agreements fulfill the goal of free trade between all countries by the end of 2010 only if all is interpreted as meaning 'almost all' and a majority of shallow agreements is acceptable. The credibility of the Barcelona Process has been damaged by the failure of the Southern Mediterranean States to enter a free trade agreement with Israel, the country with the largest GDP in the region, making an economic mockery of regional free trade area. Without making fundamental and difficult political decisions to deepen and widen the agreements, the Union for the Mediterranean is unlikely to succeed in reinvigorating the Barcelona Process.

3.2 The Eastern Partnership

The Eastern Partnership also offers the possibility for each of the six partner countries to conclude bilateral deep and comprehensive free trade agreements (DCFTA) in two dimensions – with the EU and with each other. The Commission gives priority to DCFTAs with the EU. It has not made regional free trade a condition for a bilateral agreement with the EU, as it did in the case of the Balkan countries having a SAA with the EU, nor specify a target date for this as in the Barcelona Process. One reason for this may be that intra-regional trade is significantly less important for the EaP six (5-10 %) than intra-regional trade was in the Balkan core (approx 30 %). In addition, the EaP six already have regional free trade agreements with each other, albeit very shallow ones, through participation in CIS. It is therefore unlikely that any pairs of the EaP six will conclude DCFTAs with each other for

³ Trade Commissioner Peter Mandelson describes the situation as follows in his address to the First Agadir Investment Forum, in Brussels 8 April 2008. “---creating a regional market place along the southern shore of the Mediterranean has turned out to be a political challenge of the first order. You don't need me to tell you how far away you are from ---[your] ... goals. regional integration in the Southern Mediterranean is lower than anywhere else in the world. You do not trade with your neighbours. It makes you almost unique in the world.”

some time. Only when two EaP countries with significant (potential) trade flows between them both have DCFTAs with the EC, are they likely to want to negotiate a DCFTA with each other to avoid the disadvantages of a hub-and-spoke system.

The EU invited the Ukraine to negotiate a DCFTA with it and started negotiations in February 2008. Progress was slow, in part because of increasing uncertainty surrounding political leadership in the Ukraine, in part because of insufficient technical and institutional competence in its administration concerning trade issues. Because of accumulating difficulties in these negotiations, the Commission has stressed the importance of better preparedness before starting additional negotiations.

In the course of 2008 the Commission conducted a feasibility study and fact-finding mission in Georgia. This resulted in an assessment of Georgia's preparedness for negotiating a DCFTA in March 2009. This assessment identified issues where Georgia needed to make progress in order to qualify to start negotiations. Georgia started discussions with Commission Services in the Autumn of 2009 on how to fulfill recommendations in the fields of SPS, technical regulations and standards, competition policy and intellectual property rights. Progress has been slow in these discussions and negotiations now appear unlikely to start in 2010.

The Commission conducted a similar feasibility study in Armenia in Spring 2008 and a fact-finding mission in Spring 2009 and presented its assessment in May 2009. Armenia is thus behind Georgia in this process.

The Commission conducted a feasibility study in Moldova in fall 2009 and a fact finding mission in Spring 2010. It is likely to present its assessment in Summer or Autumn 2010. Discussions with Moldova on how to fulfill the key recommendations can be expected to start thereafter. The new Moldovan Government has expressed its interest in a DCFTA.

Azerbaijan and Belarus are not WTO members yet, one precondition for a DCFTA.

While the EU started negotiations with Ukraine quickly, they soon ground to a halt as the preparedness of Ukraine became apparent. Consequently, it is taking longer than anticipated, for Georgia to convince the Commission that it is prepared to start negotiations. Armenia and Moldova are likely to be even less prepared. It therefore seems clear that the start of negotiations with these countries will be significantly staggered. While reducing the pressure on scarce Commission resources, this does mean that benefits from coordination and cooperation will be more difficult to realize.

3.3 The Prospects for Success

The Barcelona Process has a longer track record than that of the Eastern Partnership, making it easier to assess. There is no indication at present that the Union for the Mediterranean is prepared to take political initiatives to include Israel in the core free trade area or to deepen the numerous shallow free trade agreements. As yet it has only added another layer of bureaucracy without reinvigorating the Barcelona Process. This suggests that any initiative to 'reinvigorate' the Barcelona Process will have to come from the northern shore of the Mediterranean.

Although it is too early to evaluate the start of the Eastern Partnership, some reflections may be in order. Somewhat surprisingly, there was no immediate rush to start negotiations for DCFTAs.

Belarus and Azerbaijan did not qualify for consideration at the outset on several grounds. Moldova and Armenia were initially skeptical. Ukraine and Georgia responded positively but failed to get off to a flying start. A number of reasons might explain their failure.

First, their basic motivation for a DCFTA was political rather than economic. The decision to open negotiations with Ukraine was made following the enthusiasm generated by the Orange Revolution. Georgia, originally satisfied with a shallow agreement, opted for a DCFTA after the August 2008 war with Russia. In both cases, the DCFTA was seen as a means of improving national security in the face of an external threat and in the absence of NATO membership. While opting for a DCFTA was no doubt the right decision, it may have been made for the wrong reason – as though there were an economic quick fix to geopolitical threats to vital national interests. This mismatch between what these EaP governments really wanted and what the EU really could deliver is likely, if unresolved, to continue to cause problems.

Secondly, Ukraine and Georgia like the other EaP countries are in the early stages of transition. They lack a well-functioning market economy and the national institutions required to manage it.⁴ The efforts the governments will need to make to negotiate and implement a complex DCFTA are likely to exceed the resources and time they deem is available to them. The Eastern Partnership provides for technical and institution-building assistance. This assistance will need to be activated already before negotiations start in order to enable any EaP country even to qualify for negotiations.

Thirdly, and partly as a result of the above, countries have underestimated the cost and the time required to negotiate and to implement a DCFTA. The negotiations with Ukraine bogged down rather quickly as it became apparent that the government was ill-prepared to undertake a wide range of highly technical commitments. Some countries appeared surprised by the need to deal at the outset with a vast range of unfamiliar technical nuts and bolts of trade policy. Others discovered that there is no room for negotiating a special deal. The substance of a DCFTA cannot differ from country to country. The main issues open to negotiation is the length of transition periods and the amount of technical assistance required to meet the conditions set by the EU for a DCFTA. Entering the discussions with unrealistic expectations understandably led to disappointments and frustrations.

Does the failure to get off to a flying start mean that a DCFTA is too ambitious a goal for the EaP countries? Not necessarily. A DCFTA is an effective instrument of economic modernization. It will accelerate the country's transition to a functioning market economy. It provides access to the EU single market allowing the EaP countries to diversify the country and commodity composition of their trade. Sooner or later the country must undertake this transition. It is better that it take place sooner rather than later. It does mean though that it will be a time-consuming and difficult process. In this, as in all educational processes, encouragement is the best didactic method. The EaP countries need encouragement.

To improve the prospects of success, the EaP governments and the EU must improve their common understanding of what the Eastern Partnership can and cannot deliver; the Ea P countries will need to focus their efforts on building institutions to manage market economies while the EC will need to mobilize significant financial and technical resources to help them do this; and finally the Ea P

⁴ A thought provoking illustration of the difficulties is provided by Thorvaldur Gylfason and Eduard Holchreiter (2008).

governments will need to understand that the Eastern Partnership does not provide a quick fix for geopolitical problems but requires dealing with the tedious nitty gritty of trade policy. Even under these circumstances it could take up to five years for the two EaP countries that have started the process to conclude their DCFTAs. The prospect of accession could speed this up.

4. The Importance of Soft Power

Soft power is the ability to get one's partners themselves to want to do what you want them to do. Without soft power, a government must use hard power to get its partners to do what it wants them to do. Hard power is expensive since it requires offering rewards and/or making threats in order to get your way. What is the proper mix of hard and soft power in the EU's relations with the countries of the Eastern Partnership and Southern Mediterranean, respectively.

4.1 The Prospect of EU Accession

A good illustration of the effective use of soft power is provided by how the prospect of EU accession enticed the Balkan countries to establish a free trade area. In order to encourage post-war reconciliation in the former Yugoslavia, the Stability Pact proposed in January 2001 that the Balkan governments negotiate a free trade agreement. This proposal met with skepticism. Each Balkan country feared that this was an alternative to accession to the EU – its key priority. With ill-concealed reluctance, the countries nevertheless agreed to enter individual bilateral agreements with parties of their choosing. Even though the EU at the outset required any country in the Balkans with a Stabilisation and Association Agreement (SAA) with the EU, to enter a free trade agreement with other countries that had SAAs, this had little effect. The network of bilateral free trade agreements grew rather slowly. Only when the EU made clear that regional free trade was a precondition for accession, did the Balkan countries start to listen. And it required the European Council to declare at its meeting in Thessaloniki in June 2003 that the future of the Western Balkans lay in the European Union to convince the ex Yugoslavia countries that accession was a credible prospect for them.

Accession had a compelling logic of its own. The EC representative in the Trade Working Group made it clear, gently but firmly, that no single country could accede to the Union with unresolved conflicts with its neighbours. Should it enter the EU alone, these conflicts would become EU conflicts with a third party. Should it enter the EU with its neighbours, these conflicts would become EU- internal conflicts. Neither alternative was acceptable.

In the next couple of years the countries replaced the network of bilateral free trade agreements with a single free trade agreement encompassing all countries (CEFTA 2006). Towards the end of the negotiations the countries were competing to harmonise their legislation on the EU *acquis*. They called the new agreement CEFTA in order to signal that they saw CEFTA as a vehicle leading them to EU membership following in the tracks of former CEFTA members which joined the EU in 2004 and 2007.⁵ Trade Commissioner Peter Mandelson urged the Balkan countries to see CEFTA 2006 as “a training ground” for future membership in the European Union.

⁵ Countries in the Western Balkans submitted applications for EU membership in the following order: Croatia 21 February 2003; Macedonia 15 December 2005 (?); Montenegro 15 December 2008; Albania 28 April 2009; Serbia 22 December 2009.

Will this strategy work for the countries of the Eastern Partnership? Probably not. Intra-regional trade between the EaP countries, with the possible exception of trade between Georgia and Armenia and between Moldova and Ukraine, is hardly sufficient to motivate them to negotiate a deep free trade agreement. Two other considerations are more important. The first is that their driving force for a bilateral agreement with the EU appears to be strategic rather than economic. The second is that unresolved conflicts in this region will require more than regional free trade inspired by the promise of EU accession to be resolved. Consider these in turn.

First, while EU membership improves national security even without NATO membership (cf the Baltic States), a DCFTA without the prospect of EU membership is less likely to. Thus, the EaP countries may be hesitant to invest the significant resources required to negotiate and implement a DCFTA with the EU. If so, the EU must make it clear at the outset that the countries of the Eastern Partnership are eligible for membership subject to the standard qualifications. Ambiguity about the limits of Europe is not constructive.

Second, regional conflicts (Transnistria, Abkhazia, South Ossetia) primarily involve a third party – Russia – which is impervious to EU's soft power, not being a candidate for accession to the EU. Here only hard power will be effective. The conflict between Armenia and Azerbaijan over Nagorno-Karabakh involves also Turkey. If both Turkey and Azerbaijan were candidate countries, the prospect of accession might increase their willingness to help resolve this conflict. At least for now, this is not the case.

This suggests that negotiating a bilateral DCFTA with the EU is likely to be an excessively costly task without the prospect of EU membership. Even if it succeeds, regional free trade by itself will be insufficient to resolve the conflicts in this region.

4.2 The Importance of Institution building

“Rien n'est possible sans les homes, rien n'est durable sans les institutions.” Monnet, Mémoires, s. 441.

It follows that assistance to EaP countries to build institutions for conducting trade policy is essential for success. Strong institutions can endow good substance with longevity. Weak institutions can kill it at once. The institutions that the Stability Pact set up to negotiate regional trade agreements over a period of six years helped put the Balkan countries on the track to EU accession. The hard work was done in the Stability Pact's Trade Working Group where civil servants from participating ministries of trade and/or economy met about four times a year during the six years. This provided an occasion for neighbours long separated by the Cold War to get to know each other and former adversaries, often with bitter personal memories of fratricidal wars, to sit down and discuss common problems. The location of the meetings rotated between the participating countries, now sovereign States. Slowly but surely the meetings built confidence among participants. Civil servants reported to and took instructions from their Ministers and these met at least once a year to confirm what their civil servants had agreed upon, resolve possible disagreements and give new instructions.

The Trade Working Group was part of the Stability Pact's institutional structure. It reported to Working Table II of the Stability Pact which in turn reported to its Regional Table (at Ministerial Level) which met twice a year. The donor countries participated in this structure and could continually

monitor developments and provide moral and financial support. This institutional structure effectively formulated instructions, set time tables, provided proper reporting, ensured accountability at various levels and exercised peer pressure. The 'accountability' of the Region's Ministers towards the international communities' representatives in the Stability Pact was a precondition for support. Eventually, this set in motion a virtuous cycle.

The Trade Working Group's proposal to replace the network of bilateral agreements by a single regional agreement had an important institutional implication. Bilateral agreements are managed by Joint Committees with representatives of the two participating governments. Plurilateral agreements are normally managed by institutions where all parties participate. The dynamics of decision making is completely different in the two alternatives; the one adversarial the other co-operative. A key controversy in the Stability Pact concerned whether or not to set up a secretariat to manage the new regional agreement (CEFTA 2006). The secretariat services for the old CEFTA were provided by the country in the geographically rotating Chair. Especially the smaller countries argued that the new CEFTA required a permanent secretariat since CEFTA 2006 was more ambitious and complex than the old CEFTA. A permanent secretariat could provide an institutional memory and thereby historical continuity, guarantee impartiality and provide a common resource dedicated only to this task. These arguments carried the day. While CEFTA is a standard international organisation with no sharing of sovereignty, its common institutions helped to convert adversarial relationships into a cooperative venture.

Negotiating regional free trade was a time consuming process, taking altogether 6 years in an iterative process. For most countries it preceded the negotiation of the bilateral SAA with the EU and in fact served as a warming-up exercise for these.⁶ In the case of EaP countries, this order is reversed with the DCFTAs with the EU coming before the regional FTAs. This forces the EaP countries to build effective national institutions quickly. How long this will take will depend critically on how soon the EaP countries can receive assistance to do this.

The Eastern Partnership foresees that the Commission will fund a Comprehensive Institution Building programme (CBI) to assist the partner countries to build national institutions necessary for implementing the DCFTAs. The candidates will need assistance in setting up independent Competition Authorities and Public Procurement Bodies, institutions to monitor and enforce Food Safety and Quality laws and regulations, effective Customs Offices monitoring complex rules of origin, Judicial bodies and procedures to enforce intellectual property rights, etc. Given the limited experience of the EaP six with these issues, this will prove to be a major and costly task. Financial assistance (hard power) will be necessary.

In addition, the Eastern Partnership foresees a multilateral framework to negotiate the Ea P and to manage the new regime. The Commission proposes a common institutional structure somewhat similar that of the Stability Pact. Prime Ministers will meet every other year and Foreign Ministers annually. Four thematic platforms will deal with Democracy and governance stability, Economic integration and EU convergence, Energy Security and Contacts People respectively. The Commission will prepare the agendas and chair the meetings (as the Stability Pact chaired its three Working

⁶ Macedonia signed SAA 9 April 2001, in force 1 April 2004; Croatia 29 October 2001 (1 February 2005); Albania June 2006 (1 April 2009); Montenegro 15 October 2007; Serbia 29 April 2008 (7 December 2009); Bosnia-Herzegovina 12 June 2008. In most cases, the agreements were applied provisionally until entry into force.

Tables. Panels can be set up as needed with format and participation to be decided from case to case. The Panels are similar to the Working Groups in the Stability Pact. Thematic working groups can be set up at a technical and civil servant level. It is more effective and less expensive to hold these meetings on a plurilateral rather than bilateral framework. However, given that the starting dates for negotiations with the various EaP governments can be expected to be widely staggered, timing these activities may prove difficult.

Once a network of bilateral DCFTAs has been created in the region the Commission proposes creating a Neighbourhood Economic Community (NEC), as an expression of joint ownership by the EU and the EaP countries of the management of the free trade area. The Commission refers to the institutions forming the European Economic Area created by the EFTA countries and the EU in 1994. This would require the participating EaP countries to create a “second pillar” consisting of a surveillance authority and a court. This expense might be justified if the the EaP participants do not have a membership perspective. If they do, it might be more efficient to expand the already small EEA institutions with EaP institutions and representatives. This would allow the EaP countries to benefit from the experiences and knowledge of the EFTA participants and avoid institutional duplication.

5. The Need for Hard Power

Hard power in the form of carrots and/or sticks will be necessary in both geographic parts of the European Neighbourhood Policy and place significant demands both on the budget and on the foreign and security policy of the European Union.

Even if the EaP countries have a membership prospect, resolutions of conflicts in the EaP (Transnistria, Abkhazia South Ossetia) cannot be solved by soft power alone since they are in conflict with a third party (Russia). The EU will also need to fund the institutional structure (NEC) set up to manage the Eastern Partnership co-operation. Hence, hard power will be necessary to elicit the cooperation of involved parties. Since the countries of the Southern Mediterranean cannot – without revision of Article 49 - have a membership perspective, the EU must find strong incentives if it wishes to encourage them to enter deep and comprehensive agreements with each other as a means to resolve regional conflicts.

The costs in terms of money and goodwill to deliver results in both these regions will be great and substantially exceed what the EU is willing or able to pay. Any serious attempt at conflict resolution in any part of the European Neighbourhood will therefore require the participation of additional donor countries.

5.1 The Resolution of Regional Conflicts

Two major conflicts dominate the Mediterranean: that between the State of Israel and the Palestinian Authority, and that between Morocco and Algeria concerning West Sahara. Of these the first is a long-festering conflict, directly involving neighbours and indirectly involving many others, which the parties have proved incapable of resolving themselves. What carrots and/or what sticks can outsider wield to assist the parties to make the transition from trade embargos to free trade?

When it started in 1995, the Barcelona Process was fueled by optimism generated by the Madrid Conference of 1991, the Oslo Accords of 1993 between Israel and the PLO and the Israel-Jordan

Peace Treaty of 1994. However, Israel and the Palestinian Authority failed to reach a final settlement at the Camp David Summit in 2000 and thereafter hostilities between Israel and Palestinians increased. It would be too easy to blame the failure of the Barcelona Process on the renewed hostility induced by the immediate parties to the conflict. Outside mediators are often necessary to help the parties to a conflict to take the first steps to convert a vicious circle into a virtuous one. This was presumably one of the objectives of the Barcelona Process. What initiatives could the outsiders take?

A logical economic first step would be for outsiders to encourage the four signatories of the Agadir Declaration to invite Israel to join that agreement. Egypt (in 1979) and Jordan (in 1964) have signed peace treaties with Israel. They are the only PAFTA countries to have trade agreements with Israel, albeit not free trade agreements. Morocco and Tunis have diplomatic/good relations with Israel (??). It would be natural for Egypt, Israel and Jordan, three contiguous countries, to trade extensively with each other. An Agadir Group that included Israel could expand to the considerable benefit of its neighbours. Lebanon is one of the richer countries in the region and the trade potential between Israel and Lebanon is large. Open borders would in particular benefit the occupied Palestinian territories providing access to Egypt and Lebanon.

These four contiguous countries either have DCFTAs with each other and with the EU or could rather easily negotiate them. A common institutional framework such as the Neighbourhood Economic Committee (NEC) as proposed by the Commission and encompassing both the EU and Agadir governments could anchor the agreement politically and provide additional economic benefits to the most advanced economies in the southern Mediterranean.

The economic sense of a NEC encompassing the Adadir four plus two is overwhelming. Equally overwhelming is the political sense that a solution to the plight the Palestinian refugees, now numbering now about 4,5 million (including their living descendants) is a precondition. However, providing them with decent living conditions and opportunities for self-sustaining jobs will cost sums comparable to the Marshall Plan in real terms. The immediate parties to the conflict will not/cannot finance the costs themselves. Outsiders will need to contribute. Outside donors (the quartet) will need to contribute about 100 billion dollars to create the political preconditions for a settlement which could spark economic prosperity in the region.

Little imagination is needed to understand that resolution of the conflicts in the EaP will similarly require significant side payments in some form or another.

5.2 Funding the new institutions

The EU funds currently foreseen for this task are likely to prove insufficient. The level of ENPI support for Eastern Europe in 2009 (€450 million per year) will rise to €785 million during the budget period 2010-2013 and perhaps to €1.5 billion annually in the period 2014-2020. Competing claims from new members, from the Pre-Accession fund and from the Southern Mediterranean countries in the ENP will inevitably limit the amount available for Ea P countries. By comparison, the EU provided about €1 billion annually to the Western Balkans in the period 2000-2006. The six Ea P countries will need more assistance than what the Western Balkan countries received.

Additional funds must therefore be mobilized from other sources. The international financial institutions (World Bank, EBRD, EBI) will no doubt contribute. The WTO can train civil servants in basic WTO rules and procedures. But ultimately EU Member States will have to contribute through their national bilateral assistance programmes. A key element for success is that those EU Member States that have a special interest in the Ea P countries will have to take the initiative to co-ordinate efforts and leverage them so as to provide more technical and financial assistance to the Ea P six than can be foreseen in the EU budget.

If and when a sufficient number of EA Partner countries have entered DCFTAs with each other, the Commission's proposal foresees the creation of a Neighbourhood Economic Committee (NEC) as a multilateral governing body with representatives from both sides. The Commission's communication makes a reference to the EEA institutional structure in this context. This would require the participating Ea P governments to create a second pillar. It makes little sense to create new institutional structures if the Ea P participants have a membership perspective and participation in the NEC can be expected to be temporary. In this case, it makes more sense to use the existing structures of the EEA. Why reinvent the wheel? A new NEC structure can only be justified as a home for participants with no prospect of membership.

5.3 The Need for Donor Co-operation

Given the costs that can be foreseen and the number of outsiders with interests in the European Neighbourhood, the EU will need to co-operate with other donor countries to exercise the hard power necessary to reconcile the parties. The Stability Pact provides a model for this. Within that framework the EU was not alone, although it played a lead role, but was assisted by the USA, Norway and Switzerland in providing moral support and financial support. EU Member States with a special interest in the region were also active. International institutions such as the World Bank and the WTO were important actors. Participation by all of these significantly leveraged the contributions of the EU.

Outside actors such as the United Nations, Russia and the USA will need to be involved to solve the conflicts in the Middle East and in Moldova and the Caucasus. The massive funding necessary for a serious attempt to deal with these issues will require a significant inputs from these outsiders in addition to anything that the EU puts in.

6. Conclusion

Formulating and executing the ENP requires taking an extremely long view. It will take time to 'overcome' the many factors contributing to 'enlargement fatigue' that will plague the EU for some time. It will take time for the EU's neighbours to make the transition to functioning market economies and build the national institutions necessary to negotiate and implement deep and comprehensive free trade agreements. Both current and prospective members will need time to overcome these difficulties. The EU, together with other donors, will also need to contribute significant resources to these ends. Most importantly, they will need statesmanship and perseverance if they are to resolve the regional conflicts which can easily degenerate to great power confrontations. Proximity to these powder kegs forces the EU in its own self interest to take a leadership role in addressing these issues in its neighbourhood.

Bibliography

Baldwin, R. E., *Towards an Integrated Europe*, CEPR, London, 1994.

Gylfason, Th. and Hochreiter, E., Growing Apart? A Tale of Two Republics: Estonia and Georgia, IMF Working Paper (WP/08/25). [find published source]

Gylfason, Th. and Wijkman, P.M., *Turkey's Road to Europe*, Vox.

Hoekman, B. and Messerlin, P., "Initial Conditions and Incentives for Arab Economic Integration: Can the European Community's Success be Emulated?" in Galal, A. and Hoekman, B. (ed), *Arab Economic Integration: Between Hope and Reality*, Brooking Institutions Press, Washington D.C., 2003.

Hufbauer, C.G. and Brunel, C., *Maghreb Regional and Global Integration: A Dream to be fulfilled*, Peterson Institute for International Economics, Washington, D.C., 2008.

Lamy, P., Terrorism and Global Trade Rules, Presentation to Institute for Graduate Studies September 2007.

Monnet, J., *Mémoires*, Librairie Arthème Fayard, 1976.

Wallace, H., *The European Union and its Neighbourhood; Time for a Rethink*, ELIAMEP, May 2009.

Wallace, W., *Looking after the Neighbourhood: Responsibilities for the EU-25*, [ref]

Wijkman, P.M., *Frihandel för fred: Exemplet Balkan*, SNS, 2009.