

Marek Dabrowski
Maryla Maliszewska *Editors*

EU Eastern Neighborhood

Economic Potential and
Future Development



Springer

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Editors

Prof. Dr. Marek Dabrowski
Center for Social & Economic Research
(CASE)
ul. Sienkiewicza 12
00-010 Warsaw
Poland
marek.dabrowski@case-research.eu

Dr. Maryla Maliszewska
Center for Social and Economic Research
(CASE)
ul. Sienkiewicza 12
00-010 Warsaw
Poland
Maryla.Maliszewska@case-research.eu

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Preface

This volume contains a selection of research output from the Specific Targeted Research Project (STREP) on 'EU Eastern Neighborhood: Economic Potential and Future Development (ENEPO),' which was funded under the EU Sixth Framework Program, Priority 7 'Citizens and Governance in a Knowledge Based Society', Contract No 028736 (CIT5).

The main objective of the ENEPO project was to examine the potential of the ENP and the EU strategic partnership with Russia to upgrade relations between the enlarged EU and CIS countries in the spheres of trade, investment, labor movement, technical cooperation, and economic and governance reforms in the CIS, with special attention given to mutual interdependence among these cooperation areas.

In this volume we use the term 'Commonwealth of Independent States' and its abbreviation, CIS, purely for analytical convenience in order to define the group of 12 successor countries of the former USSR (all former Soviet republics except for the Baltic states, which are now EU members). We are aware that the role of the CIS as a regional integration block, founded at the end of 1991 in order to provide a 'velvet divorce' from the former USSR, is gradually decreasing. Furthermore, in August 2009, Georgia terminated its membership in the CIS.¹

Before the launch of the ENEPO project, the vast majority of previous studies in the areas of trade, investment, and labor migration focused on the economic integration of CEE with the EU, leaving EU cooperation with the CIS outside of the main stream of analysis. With the EU's Eastern Enlargement in 2004 and 2007, research interests have evolved towards analyzing the economic relations of the entire EU27 with their new neighbors to the East.

In the governance sphere, a large body of research has focused on the post-communist transition of individual CIS countries and the CIS region as a whole, as well as cross-country and cross-regional comparative analyses. However, few

¹The analyzed group of countries has been sometimes referred to as the New Independent States (NIS). However, as almost 20 years have passed since the end of 1991 when they obtained independence, this notion also seems inaccurate.

studies have attempted to analyze the role of the European integration process as the potentially most powerful factor determining the success or failure of building a market economy and democratic society in the post-communist world. Few researchers have investigated the adoption of European economic, legal and political institutions by CIS countries, the appropriateness of these institutions to CIS development needs, and their potential to speed up the transition and modernization processes in this region.

The ENEPO project broke with the narrow focus of the majority of previous studies and concentrated on achieving the following specific objectives:

- Analysis of the development gap between CIS and EU countries
- Analysis of trade flows (including energy resources) and implications of free movement of goods and services between CIS countries and the EU
- Analysis of the sources of and obstacles to capital movement between CIS countries and the EU
- Exploration of the actual and potential labor migration and, more generally, free movement of people, and their implications for CIS and EU countries
- Identification of the governance gap between CIS and EU institutions and the differences in CIS laws and regulations with respect to the *acquis* as well as the potential role of the EU and ENP in closing the discrepancies
- Drawing policy recommendations related to reform strategies in CIS countries and further development of the ENP and related EU policies towards its Eastern neighbors

The innovative approach of the ENEPO research agenda consisted of a deeper investigation of the interrelations between the above-mentioned economic cooperation and policy reform areas along with an underlying assumption of a far-going interdependence between progress achieved within each area of integration.

The thematic outline of this volume largely follows the above list of research objectives. In the Chap. 1, Irina Sinitsina identifies various dimensions of the development gap between CIS countries and the EU. In Chap. 2, Arne Melchior brings a geographical economics perspective to the analysis of the income gap and cohesion processes in Europe as a result of the increasing economic integration of the continent. Maryla Maliszewska, Iryna Orlova and Svitlana Taran introduce the concept of 'deep' trade and economic integration in Chap. 3 and estimate the impact of the removal of non-tariff barriers between the EU and selected CIS partners. In Chap. 4, Wojciech Paczynski and Vladimer Papava concentrate on a strategically important component of EU-CIS trade relations, namely energy supply and transit. Alina Kudina and Malgorzata Jakubiak provide an empirical analysis of the dominant foreign direct investment (FDI) strategies and major obstacles to FDI in selected CIS economies in Chap. 5. In Chap. 6, Vladimir Borgy and Xavier Chojnicki assess the demographic and economic consequences of migration in Europe and neighborhood countries in the context of population aging, using a multi-regions CGE-OLG model INGENUE2. Matthias Luecke continues the migration topic in the following Chap. 7, concentrating his analysis on the direct and indirect income effects of international labor migration and remittances in

selected CIS countries. In Chap. 8, Inna Melnykovska and Rainer Schweickert analyze the external determinants of institutional change in transition economies such as the EU and NATO membership perspectives, association and trade agreements with the EU, and WTO membership. The topic of institutional change is continued in Chap. 9, in which Anna Kolesnichenko discusses the concept of institutional harmonization and its potential benefits and costs for EU neighbors. In Chap. 10, Roman Mogilevsky and Aziz Atamanov focus on the role of technical assistance (especially that which is provided by the EU) in fostering the economic and institutional transformation of CIS countries. In Chap. 11, Wojciech Paczynski discusses the current and potential role of the ENP in anchoring economic reforms in CIS countries. In the final Chap. 12, Marek Dabrowski provides an overview of EU-CIS economic relations and EU policies towards this region, bringing together the analysis and conclusions of the entire volume.

The contributions published in this volume are based on earlier, much larger versions of research papers and reports prepared within the ENEPO project. They were, however, subject to re-editing and updating in late 2010 and early 2011, taking into account the most recent developments in the analyzed areas.

The ENEPO project itself was conducted from May 1, 2006 until April 30, 2009 by a consortium of 11 research institutes led by CASE – Center for Social and Economic Research in Warsaw. Apart from CASE, the consortium consisted of Center for Economic and Financial Research CEFIR in Moscow, Center for Social and Economic Research CASE-Kyrgyzstan in Bishkek, Center for Social and Economic Research CASE-Transcaucasus in Tbilisi, Center for Social and Economic Research CASE Ukraine in Kiev, Centre d'Etudes Prospectives et d'Informations Internationales CEPII in Paris, Centre for European Policy Studies (CEPS) in Brussels, Foundation for Social and Economic Research CASE Moldova in Chisinau, Institute for Market Economics (IME) in Sofia, Kiel Institute for the World Economics (IfW) in Kiel and Norwegian Institute of International Affairs (NUPI) in Oslo.

The editors of this volume, who also acted as the scientific coordinators of the ENEPO project, would like to express their gratitude to all participating institutes, their researchers, and administrative staff. The editors would like to especially acknowledge CASE Vice-President Sebastien Leclef, who effectively managed the ENEPO project through its entire life span. Special thanks go to Paulina Szyrmer, who provided detailed editorial support in preparing this volume.

Needless to say, all the views, opinions and policy recommendations presented in this volume are those of the respective authors only and do not necessarily reflect the position of the project donor (European Commission), project institutional participants, institutions which the authors have worked for or have been associated with, and other contributors to ENEPO project and this publication.

March 9, 2011

Marek Dabrowski
Maryla Maliszewska

List of Abbreviations

ACAA	Agreement of Conformity Assessment and Acceptance
ADB	Asian Development Bank
bcm	billion cubic meters
bn	billion
BoP	Balance of Payments
CA	Central Asia
CE	Central Europe
CEE	Central and Eastern Europe
CES	Constant Elasticity of Substitution
CGE	Computable General Equilibrium (Model)
CGE-OLG	Computable General Equilibrium Overlapping-Generation (Model)
CIS	Commonwealth of Independent States
COMECON	Council for Mutual Economic Assistance (CMEA)
CWB	(EU) Candidates and Western Balkan Countries: Albania, Bosnia & Herzegovina, Croatia, Kosovo, Macedonia, Montenegro, Serbia, Turkey
DCFTA	Deep and Comprehensive Free Trade Agreement/s
EA	Europe Agreement/s
EAAP	Europe Agreement Additional Protocol/s
EaP	Eastern Partnership
EBRD	European Bank for Reconstruction and Development
ECA	Europe and Central Asia
EE	Eastern Europe
EEN	Eastern European Neighbors
ENEPO	EU Eastern Neighborhood: Economic Potential and Future Development (FP6 Funded Project)
ENP	European Neighborhood Policy
ENP AP	European Neighborhood Policy Action Plan/s
ENPI	European Neighborhood and Partnership Instrument
EPI	Environmental Performance Index

EU	European Union
EU10	EU12 Minus Bulgaria and Romania
EU12	See NMS
EU15	Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxemburg, Netherlands, Portugal, Spain, Sweden, United Kingdom
EU25	All Member States of the EU Since 2005 (EU27 Minus Bulgaria and Romania)
EU27	All Member States of the EU Since 2007 (EU12+EU15)
EUR	Euro
FDI	Foreign Direct Investment
FE	Fixed Effects (Estimator)
FSU	Former Soviet Union
FTA	Free Trade Agreement/s
GAMS	General Algebraic Modeling System
GDN	Global Development Network
GDP	Gross Domestic Product
GOST	<i>Gosudartvennyi Standard</i> (State Standard)
GSP	Generalized System of Preferences
GTAP	Global Trade Analysis Project
HBS	Household Budget Survey/s
HME	Home Market Effect
IFC	International Financial Corporation
IFPRI	International Food Policy Research Institute
ICT	Information and Communication Technologies
IMF	International Monetary Fund
ITGI	Interconnection Turkey-Greece-Italy
JHA	Justice and Home Affairs
KAM	Knowledge Assessment Methodology
LNG	Liquefied Natural Gas
MAP	Membership Action Plan (in NATO)
MENA	Middle East and North Africa
M&E	Monitoring and Evaluation
MFN	Most-Favored Nation
mn	million
MNE	Multi-National Enterprise/s
MTO	Money Transfer Office/s
NBKR	National Bank of the Kyrgyz Republic
NGO	Non-Governmental Organization/s
NMS	New Member States of the EU: Bulgaria, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovakia, Slovenia
NACE	<i>Nomenclature Statistique des Activités Économiques</i> (Statistical Nomenclature of Economic Activity)

NAFTA	North American Free Trade Agreement
NATO	North Atlantic Treaty Organization
NEG	New Economic Geography
NTB	Non-Tariff Barriers
NUTS	Nomenclature of Territorial Units for Statistics
ODA	Official Development Assistance
OECD	Organization for Economic Cooperation and Development
OLS	Ordinary Least Squares (Regression)
PAYG	Pay-As-You-Go (Pension System)
PCA	Partnership and Cooperation Agreement/s
PISA	Program for International Student Assessment
POLS	Pooled Ordinary Least Squares (Regression)
PPP	Purchasing Power Parity
R&D	Research and Development
SAA	Stabilization and Association Agreement/s (with the EU)
SAM	Social Accounting Matrix
SEE	South Eastern Europe
SPS	Sanitary and Phyto-Sanitary (Measures)
TA	Technical Assistance
TAA	Trade and Association Agreement/s
TAP	Trans Adriatic Pipeline
TACIS	Technical Assistance to the Commonwealth of Independent States
TB	Tuberculosis
TC	Technical Cooperation
TPF	Total Factor Productivity
UK	United Kingdom
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nation Development Program
UNESCO	United Nations Educational, Scientific and Cultural Organization
US	United States (of America)
USD	United States Dollar
USSR	Union of Soviet Socialist Republics
VAT	Value Added Tax
WB	World Bank
WBGI	World Bank Governance Indicators
WDI	World Development Indicators
WE	Western Europe
WHO	World Health Organization
WITS	World Integrated Trade Solution
WTO	World Trade Organization

Contributors

Aziz Atamanov PhD student at the Maastricht Graduate School of Governance; Economist at CASE-Kyrgyzstan in Bishkek, AzizAtamanov@hotmail.com

Vladimir Borgy Economist at the Banque de France (Monetary and Financial Analysis Directorate), previously worked at CEPII in Paris and for the French Ministry of Economy, Finance and Industry, Vladimir.Borgy@banque-france.fr

Xavier Chojnicki Research Fellow at CEPII in Paris; Associate Professor of Applied Economics at the University of Lille 2, Xavier.Chojnicki@univ-lille2.fr

Marek Dabrowski Co-founder and President of CASE, former Deputy Minister of Finance of Poland (1989–1990), policy consultant to governments and central banks of more than 20 transition and developing countries, Marek.Dabrowski@case-research.eu

Małgorzata Jakubiak Economist at the Directorate General for Trade of the European Commission, previously worked as an Economist at CASE (1997–2008) and served as CASE Vice-President (2007–2008), Malgosia.Jakubiak@gmail.com

Anna Kolesnichenko Economist at UniCredit/Bank Austria in Vienna; Research Associate at CASE Ukraine since 2001, Anna.Kolesnichenko@unicreditgroup.at, akolesn2@yahoo.com

Alina Kudina CASE Fellow; Research Associate at CASE Ukraine (since 1998); Assistant Professor of International Business at Warwick Business School; Associate at the UK's Advanced Institute of Management Research, alina.kudina@wbs.ac.uk

Matthias Luecke Senior Research Economist at the Kiel Institute for the World Economy and Adjunct Professor at Kiel University; Senior Economist at the International Monetary Fund (2000–2003), Matthias.Luecke@ifw-kiel.de

Maryla Maliszewska Economist at the World Bank; Economist at CASE (1996–2010) and CASE Fellow specializing in macroeconomic and trade policy related issues, Maryla.Maliszewska@case-research.eu

Arne Melchior Senior Research Fellow at the Norwegian Institute of International Affairs (NUPI) in Oslo; previously served as the Assistant Director and Head of Department at NUPI, Arne.Melchior@nupi.no

Inna Melnykovska Research Associate in the Department of Political Science at the Christian-Albrechts-University of Kiel; Research Fellow at the Kiel Institute for the World Economy, Inna.Melnykovska@politik.uni-kiel.de

Roman Mogilevsky Executive Director of CASE-Kyrgyzstan in Bishkek and CASE Fellow, Roman.Mogilevskii@gmail.com

Iryna Orlova Economist at CASE Ukraine in Kyiv, IOrlova@case-ukraine.kiev.ua

Wojciech Paczynski CASE Fellow and Member of the Supervisory Board of CASE Ukraine in Kyiv, CASE Economist since 2000, Wojciech.Paczynski@case-research.eu

Vladimer Papava Senior Fellow at the Georgian Foundation for Strategic and International Studies, member of the CASE Advisory Council, former Minister of Economy (1994–2000) and former Member of the Parliament of Georgia (2004–2008), PapavaVladimer@gfsis.org

Rainer Schweickert Research Fellow at the Kiel Institute for the World Economy, Rainer.Schweickert@ifw-kiel.de

Irina Sinitsina CASE Fellow and the Leading Researcher at the Institute of Economics, Russian Academy of Sciences, Irina.Sinicyna@case-research.eu

Svitlana Taran Economist at the Bureau for Economic and Social Technologies (BEST) in Kyiv; Economist at CASE Ukraine in Kyiv (2007–2008), Svtaran@gmail.com

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