

European Neighborhood

Editors

Dr. Hanna Shelest
Dr. Mykola Kapitonenko

Publisher:

Published by NGO "Promotion of Intercultural Cooperation" (Ukraine), Centre of International Studies (Ukraine), with the financial support of the Representation of the Friedrich Ebert Foundation in Ukraine, and the Black Sea Trust.

UA: Ukraine Analytica is the first Ukrainian analytical journal in English on International Relations, Politics and Economics. The journal is aimed for experts, diplomats, academics, students interested in the international relations and Ukraine in particular.

Contacts:

website: <http://ukraine-analytica.org/>
e-mail: Ukraine_analytica@ukr.net
Facebook: <https://www.facebook.com/ukraineanalytica>
Twitter: https://twitter.com/UA_Analytica

The views and opinions expressed in articles are those of the authors and do not necessarily reflect the position of UA: Ukraine Analytica, its editors, Board of Advisors or donors.

ISSN 2518-7481

500 copies

BOARD OF ADVISERS

Dr. Dimitar Bechev (Bulgaria, Director of the European Policy Institute)

Dr. Iulian Chifu (Romania, Director of the Conflict Analysis and Early Warning Center)

Amb., Dr. Sergiy Korsunsky (Ukraine, Director of the Diplomatic Academy under the Ministry of Foreign Affairs of Ukraine)

Dr. Igor Koval (Ukraine, Rector of Odessa National University by I.I. Mechnikov)

Amb., Dr. Sergey Minasyan (Armenia, Ambassador Extraordinary and Plenipotentiary of Armenia to Romania)

Marcel Röthig (Germany, Director of the Representation of the Friedrich Ebert Foundation in Ukraine)

James Nixey (United Kingdom, Head of the Russia and Eurasia Programme at Chatham House, the Royal Institute of International Affairs)

Dr. Róbert Ondrejcsák (Slovakia, State Secretary, Ministry of Defence)

Amb., Dr. Oleg Shamshur (Ukraine, Ambassador Extraordinary and Plenipotentiary of Ukraine to France)

Dr. Stephan De Spiegeleire (The Netherlands, Director Defence Transformation at The Hague Center for Strategic Studies)

Ivanna Klympush-Tsintsadze (Ukraine, Vice-Prime Minister on European and Euroatlantic Integration of Ukraine)

Dr. Dimitris Triantaphyllou (Greece, Director of the Center for International and European Studies, Kadir Has University (Turkey))

Dr. Asle Toje (Norway, Research Director at the Norwegian Nobel Institute)

TABLE OF CONTENTS

THE ONLY WAY TO BENEFIT FROM THE ASSOCIATION AGREEMENT IS TO ENSURE ITS SUCCESSFUL IMPLEMENTATION	3
<i>Interview with Amb. Kostiantyn Yelisieiev, Deputy Head of the Administration of the President of Ukraine</i>	
THE EASTERN PARTNERSHIP AT THE TURN OF ITS TENTH ANNIVERSARY: WHERE HAVE WE COME SINCE PRAGUE, AND WHERE TO GO NEXT?	7
<i>Pavel Havlicek</i>	
TEN-POINT MEMO ON THE REVISED EASTERN PARTNERSHIP MULTILATERAL ARCHITECTURE	14
<i>Hennadiy Maksak</i>	
EASTERN PARTNERSHIP: WHAT OPTIONS OF DEVELOPMENT ARE NEXT FOR UKRAINE?	19
<i>Oksana Dobrzhanska</i>	
EAP-EU ECONOMIC INTEGRATION: WHAT IS NEXT?	25
<i>Yurii Vdovenko</i>	
ADVANCING THE REFORM AGENDA WITHIN THE EU ASSOCIATION AGREEMENTS: COMPARATIVE ANALYSIS OF MOLDOVA, GEORGIA, AND UKRAINE ON THE ROLE OF CIVIL SOCIETY	33
<i>Andrei Iovu</i>	
THE EU TOWARDS RUSSIA IN THE EASTERN NEIGHBOURHOOD - MISSING THE STRATEGIC VISION	41
<i>Loredana Maria Simionov</i>	
WHY BELARUS HAS A DISTINCTIVE POSITION IN THE ENP	46
<i>Fatih Ekinici</i>	
EU-NATO COOPERATION: IS PESCO THE ANSWER TO THE BALANCE OF EU'S REGIONAL PRIORITIES?	55
<i>Alexandru C. Apetroe and Daniel Gheorghe</i>	

EAP-EU ECONOMIC INTEGRATION: WHAT IS NEXT?

Dr Yurii Vdovenko

Foreign Policy Council “Ukrainian Prism”

Steering Committee of the Eastern Partnership Civil Society Forum in 2016-2017

Economic cooperation was set as one of the Eastern Partnership key priorities. The basic alternative for further development of economic cooperation within the EaP and between the EaP and the EU is a two-step integration: Establishment of the Neighbourhood Economic Community of the Association Agreement signatory states; creation of the Common Economic Space of NEC with the EU. Ukraine is acting as a locomotive on promoting within the EU ideas to transform the current EaP format, so Ukrainian stakeholders have to focus their efforts on the NEC format justification and advance.¹

Economic cooperation was set as one of the Eastern Partnership’s (EaP) key priorities. The implementation of this priority was reflected at both bilateral level, in the form of a proposal made to the partner countries to set up a Deep and Comprehensive Free Trade Area (DCFTA) with the EU, and the multilateral level, in setting up governmental Platform 2 “Economic Integration and Convergence with EU Policies” embracing sectoral panels.

There are several options in further development of economic cooperation within the EaP and between the EaP and the EU. These are based on the extent of economic integration of the EaP countries both among each other and with the EU, as well as on the direction of their foreign policy. The basic alternative is a two-step integration, which will serve to enhance the economic ties of the Association Agreement signatory

countries with each other and strengthen their positions in the negotiation process with the EU through their ability to act jointly within the EaP framework: Establishment of the Neighbourhood Economic Community (NEC) of the Association Agreement (AA) signatory states; creation of the Common Economic Space (CES) NEC with the EU. At this stage, Ukraine is acting as a locomotive in promoting within the EU ideas to transform the current EaP format; so Ukrainian stakeholders have to focus their efforts on the NEC format justification and advance.

Current State

Within the EaP, its member states have de facto split into three groups based on their integration formats of cooperation:

1) Three countries (Georgia, Moldova, and Ukraine) that have DCFTA with the EU;

¹ The article is based on policy paper “The Future Economic Integration of the Eastern Partnership Countries: A View from Ukraine” by Yurii Vdovenko.

2) Two countries (Belarus and Armenia) that have joined the alternative Eurasian Economic Union (EAEU) led by Russia;

3) One country (Azerbaijan), which keeps status quo, neither entering into a DCFTA agreement with the EU nor joining the EAEU.



Integration of the three AA signatory states with the EU has resulted in reorientation of their trade flows as an effect of the DCFTAs; however, it has not been generating essential benefits so far, nor does it have a decisive impact on their general internal economic situation.

Regardless of their proclaimed foreign policy course, all of the EaP countries are oriented towards developing their trade and economic cooperation with the EU in a bilateral format. The level of ties within the EaP is low, the AA signatory states being no exception.

In the context of global economic processes, all the partner countries have experienced worsening of their internal economic situation since the EaP establishment:

- Georgia, Moldova, and Ukraine have sustained significant losses from the phasedown in cooperation with the Russian Federation (RF), which was the latter's response to the choice of a pro-European course by these countries;
- Belarus and Armenia because of the essential dependence on Russia and structural problems of national economies;

- Azerbaijan because of the changes in the world's primary markets' conditions.

Integration of the three AA signatory states with the EU has resulted in reorientation of their trade flows as an effect of the DCFTAs; however, it has not been generating essential benefits so far, nor does it have a decisive impact on their general internal economic situation. In turn, the EU has exhausted its political potential for a deeper economic integration, stressing the necessity for the partner states to channel their efforts into the AA implementation and avoiding discussions on further integration prospects.

These realities urged the Ministry of Foreign Affairs of Ukraine on 11 July 2016 to initiate a new cooperation format among the partner countries – the EaP CES. Having a common economic block formed on the European principles could be a factor able to facilitate both an improvement in the economic situation of the partner countries and intensification of their dialogue with the EU on a deeper economic integration.

Interaction with the EU

The EaP countries should consolidate their efforts in the economic field based on the principles that are in line with European models. The three basic types of the EU agreements are:

- Customs Unions (customs barriers in bilateral trade removed, common customs tariffs for third-country imports established);
- Association Agreements, Stabilization Agreements, (Deep and Comprehensive) Free Trade Areas (FTA), Economic Partnership Agreements (customs tariffs in bilateral trade eliminated or reduced);

² R. Ralev, *EU to Set up Western Balkans Regional Economic Area*, "SeeNews", 08 June 2017, [<https://seenews.com/news/eu-to-set-up-westernbalkans-regional-economic-area-571590#sthash.faY7fHID.dpuf>].

- Partnership and Cooperation Agreements (general framework for bilateral economic relations set up, customs tariffs remain as they are).

The most widespread format of those the EU offers to its partners concerns their trade relations and is formalized in a form of either ordinary FTAs or their deep and comprehensive versions.

There is a separate format for interaction with various sorts of associations. In the FTA context, its examples include agreements concluded between the EU and Central European Free Trade Agreement (CEFTA). The CEFTA is the only FTA that has a long-term future. During the 2017 Summit, the EU presented the extension of cooperation within the CEFTA framework as the establishment of a CES with these countries.

An analysis of the EaP countries' foreign economic relations (both with each other and with the EU) envisages investigating not only qualitative indicators but also the legal foundations for these relations – how much the existing formats correlate, and also, what the membership of the EaP countries is in some or other international economic association and organization.

WTO: Armenia (05 February 2003), Azerbaijan (-), Belarus (-), Georgia (14 June 2000), Moldova (26 July 2001), Ukraine (16 May 2008).

CISFTA: Armenia (17 October 2012), Azerbaijan (10 December 2003), Belarus (20 September 2012), Georgia (-), Moldova (09 December 2012), Ukraine (20 September 2012).

GUAM FTA: Armenia (-), Azerbaijan (-), Belarus (-), Georgia (10 December 2003), Moldova (10 December 2003), Ukraine (10 December 2003).

CEFTA: Armenia (-), Azerbaijan (-), Belarus (-), Georgia (-), Moldova (26 July 2007), Ukraine (-).

EU AA (FTA): Armenia (-), Azerbaijan (-), Belarus (-), Georgia (01 September 2014), Moldova (01 September 2014), Ukraine (01 January 2016).

EAEU: Armenia (02 January 2015), Azerbaijan (-), Belarus (01 January 2015), Georgia (-), Moldova (-), Ukraine (-).

From the time the EaP started functioning, Ukraine had generated a half of the EaP GDP volume before the beginning of the Russian aggression, the second and third economies being Azerbaijan and Belarus. The lowest GDP group included Armenia, Georgia, and Moldova.

Since 2013, the export volume of the EaP's largest economies (Ukraine, Belarus, and Azerbaijan), which had been generating over 90% of the EaP's export flow, has decreased. A reduction in the share of exports in the EaP countries' GDP happened in 2012, except for Belarus, where this process began in 2013. The share of exports in GDP of the EaP countries reached its highest level in 2011, when exports exceeded 46% of the GDP.

Ukraine, Belarus, and Azerbaijan accounted for about 95% of the EaP countries' exports to the EU in 2017. The trends of export reduction from the EaP to the Russian Federation first appeared in 2013-2014, and even in 2012 in the case of Ukraine. Ukraine and Belarus accounted for over 90% of exports from the EaP to Russia in 2017.

Interaction within the EaP

The level of the EaP countries' economic interaction with each other is low. According to the European Economic Integration Index in EaP, developed by the EaP CSF Working Group 2 "Economic Integration and Convergence with EU Policies", Azerbaijan and Georgia had the closest economic relations between them. At the same time, ties between the EaP countries and the EU were much closer, having the highest index between the EU and Azerbaijan.³

The distribution of foreign economic ties among the EaP countries indicates the existence of two clusters, western (Belarus, Moldova, and Ukraine) and eastern (Azerbaijan, Armenia, and Georgia), based on their historical traditions of cooperation. It also suggests the lack of purposeful development of economic relations within the EaP. The Russian Federation sanctions imposed on Ukraine and Moldova are a factor that has an impact on exports within the framework of Ukrainian-Belarusian and Moldovan-Belarusian cooperation. Belarus, which belongs to the EAEU, acts as a transit entry point for Ukraine's and Moldova's penetration into the Russian market. Georgia plays a similar role in the other cluster, since Azerbaijan and Armenia do not maintain official trade relations.

From the point of view of Ukrainian interests, there are several primary and secondary alternatives in economic cooperation development within the EaP, which are based on two main factors:

- the benefit from a deeper level of economic integration within the EaP;
- the depth of further economic integration with the EU.

When launching the EaP, the EU intended to introduce model tools of cooperation with partner countries in the region for the sake of their approximation to the EU and each other in various areas. It emphasized equal opportunities, declared access to which was through the 'more for more' approach. Attempts were made to channel efforts to formats that would be applicable to all the EaP countries and smooth out differences existing between them. The recent years

have shown the prevalence of an individual approach to each country, as reflected in the ENP flexibility concept. Statements by the EU officials are limited to the articulation of the necessity to work consistently on the AA implementation, including the DCFTA implementation, whereas any other initiatives of a deeper integration they perceive as premature.⁴

The EaP countries also mostly prefer to develop bilateral relations with the EU. The current model's potential for further deepening of the integration has been practically exhausted. In turn, the EU still advocates keeping on the EaP framework for cooperation with all of the region's countries without shifting the priority towards bilateral relations.

The European Parliament, in its address to the Council of the European Union, the European Commission, and the European External Action Service in 2017, proposed to consider an attractive 'EaP+' model, based on the highest possible common denominator, which would include joining the customs union and Schengen area, further EU internal market access, participation in other EU programmes, increased involvement in the CSDP, as well as more immediate measures such as additional unilateral tariff preferences, the abolition of roaming tariffs between the partners and the EU, and the development of high-capacity broadband; to open the 'EaP+' model to other EaP countries once they are ready for such enhanced commitments. This model must remain open also for other EaP countries, once they are ready to undertake higher commitments.⁵

³ *European Economic Integration Index in Eastern Partnership*, Polissya Foundation for International and Regional Studies, [<http://pfirs.org/produkti/book/30-european-economic-integration-index-in-eastern-partnership/3-produkti.html>].

⁴ A. Pikulicka-Wilczewska, *Mierzymy wysoko, ale jesteśmy realistami – rozmowa z Johannesem Hahnem (We Have Ambitious Goals but We Are Realists – Interview with Johannes Hahn)*, "Eastbook", 16 October 2017, [<http://www.eastbook.eu/2017/10/16/rozmowa-johannes-hahn/>].

A deeper economic integration within the EaP is a kind of a trigger to boost fulfilment of the partner-countries' aspirations for the European integration. Any attempts to limit the EaP countries' economic integration with the EU to only trade relations' development would be wrong. In that case, the matter would be only to eliminate trade barriers on the way of export and import. The existing DCFTAs with the AA signatory countries provide an extended access to the European market because of fundamental transformations and institutional changes inside the countries, not just by solving the issues of quotas and tariffs.

The EaP countries' integration with each other may not be set as an end in itself. Benefits from such integration cannot be significant, whereas trade between partner countries is still influenced by their traditional ties developed in both the western and the eastern EaP clusters. The choice of an integration model within the EaP is based on the geoeconomic factor associated with the creation of prerequisites for a deeper integration of the EaP countries with the EU. When it is taken as the basis, the following geographic configurations appear:

- three countries – Georgia, Moldova, and Ukraine – AA states;
- four countries – Georgia, Ukraine, Azerbaijan, and Moldova – GUAM;
- five countries⁶ – Azerbaijan, Armenia, Georgia, Moldova, and Ukraine;
- six countries – Azerbaijan, Belarus, Armenia, Georgia, Moldova, and Ukraine – EaP.

Keeping up the current status quo could be also considered as an alternative, but none of the partner countries is satisfied with the



A deeper economic integration within the EaP is a kind of a trigger to boost fulfilment of the partner-countries' aspirations for the European integration. Any attempts to limit the EaP countries' economic integration with the EU to only trade relations' development would be wrong

cooperation results achieved in the economic area. If the EU is inclined to freeze the achieved integration level, this position will be under constant pressure from the EaP countries, and it will encourage a dialogue aimed at finding and implementing deeper integration models.

Options for the EaP States' Integration

The basic alternatives to the deeper economic integration within the EaP framework are as follows:

1. Integration of the three AA signatory countries, which could be implemented by joining the existing initiatives or creating a new one. The deepest integration level would be the countries' accession to the European Economic Area (EEA). Another possibility would be to join the CEFTA, with or without further accession to the EEA. A NEC might be established as a counter to the existing options, with or without further accession to the EEA.
2. Integration of the four GUAM countries, which could be implemented by joining the existing initiatives or creating a new one.

⁵ *Draft Report on a European Parliament Recommendation to the Council, the Commission and the EEAS on the Eastern Partnership, in the Run up to the November 2017 Summit (2017/2130(INI))*, Committee on Foreign Affairs, 02 August 2017, [<http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-%2f%2fEP%2f%2fNONGML%2bCOMPARL%2bPE-607.922%2b01%2bDOC%2bPDF%2bV0%2f%2fEN>].

⁶ De-facto Belarus is excluded from integration processes with the EU.



Looking from the angle of economic integration with the EU, it makes sense to consider realistic options, automatically excluding Belarus and Armenia from joint integration projects, which will come into conflict with the EAEU conditions.

A limiting factor of this alternative is the stance taken by Azerbaijan. The options are similar to those mentioned above. The NEC created in this format will have the shape of GUAM FTA.

3. Integration of five countries (Azerbaijan, Armenia, Georgia, Moldova, and Ukraine) is an alternative with significant constraints in comparison with the previous one. Although, politically, Armenia aims at integration with the EU, its EAEU membership is an additional constraint from the economic point of view. Given the current situation in Azerbaijan-Armenia relations, this alternative is hypothetical and could be implemented only if Azerbaijan changes its position and if the chasms between Azerbaijan and Armenia and between the EU and the EAEU would be bridged. Therefore, consideration of potential integration models in this configuration is not expedient for the time being.

4. Integration of the six EaP countries is the most difficult alternative. On top of the constraints mentioned above, there are both political and economic challenges associated with Belarus, which is not a WTO member but is a member of the EAEU; moreover, it does not declare its European choice. Of all the hypothetical models, this configuration will actually be about EU-EAEU integration.

The current situation in the EaP should be used as a basis for identifying the most

realistic options and proposing a possible model for further economic association with the EU for each of the options.

On the one hand, consideration of the suggested alternatives should be based on a scale of benefits that could be gained, and on the other hand, it should take into account the factor of reality. The criterion for choosing the best alternative needs to be maximization, i.e., the best alternative will be the one that allows the EaP countries to reach the deepest possible economic integration level with the EU. The EaP countries' economic integration with the EU must ensure free movement of production factors and output. The choice of alternatives will be to identify a model ensuring the four freedoms between the EaP countries and the EU: free movement of goods, services, capital, and labour.

Looking from the angle of economic integration with the EU, it makes sense to consider realistic options, automatically excluding Belarus and Armenia from joint integration projects, which will come into conflict with the EAEU conditions. Involving these countries in the EU-oriented economic integration processes will narrow possibilities for other EaP countries down to the EAEU framework from the very beginning. The option envisaged in the Belarusian concept of having a CES of the EU and the EAEU is unrealistic at the moment and should be set aside. As a result, the number of alternatives is reduced to the following two:

1. Integration of the three AA signatory countries;
2. Integration of the four GUAM countries.

Feasible options under these alternatives include accession of the abovementioned EaP countries to existing economic associations or creation of new ones:

1. Accession to the EEA;
2. Accession to the CEFTA;
3. Establishment of a NEC.

Presently, Azerbaijan has limited possibilities for deepening its economic integration in both economic and political dimensions. In the former case, the cause is that the country is not a WTO member, and in the latter case, this is due to its leadership's position with respect to European integration prospects. Therefore, the further analysis will focus on the prospects of economic integration with the EU for the three AA signatory countries.

1. Of the tested practices of the EU's economic integration with non-EU countries, the EEA format is the deepest one, reaching the integration level of an economic union. In the identification of an economic integration model for the AA signatory countries, the EU's unwillingness to offer them membership prospects is a key constraint. Accession to the EEA without joining the EU will require reaching the level of EFTA member countries. This level is presently unreachable for the EaP countries in view of the critical difference in their economic and institutional development that cannot be overcome in the near future. Thus, the one-step economic integration of the AA signatory countries with the EU through their accession to the EEA is as complicated as becoming an EU member.

2. The second option is accession of Georgia and Ukraine to the CEFTA (Moldova is its member) as an already tested integration model of a common market with the EU. The CEFTA, after the first success of its members in joining the EU, is now applied for the second time to the Balkan countries that have prospects of the membership: Work is underway to form a CES with them, in which the integration level may be characterized as a common market. Since the AA signatory countries do not have the status

of prospective members, the advantage for them to be under the aegis of the CEFTA comes to nothing. If Georgia and Ukraine join the CEFTA, it will mean that the AA signatory countries are under the external umbrella and have to follow its rules in expectation of changes in the EU's integration policy. Thus, the accession to the CEFTA would not provide the AA signatory countries with any opportunities for a deeper economic integration with the EU.

3. The third option is a two-step integration:

- 1) establish a NEC;
- 2) form a CES NEC with the EU.

This option is proactive, compared to the previous one. Unlike accession to the CEFTA, the NEC establishment has an advantage of giving the three countries the liberty of choice: how to build it and promote their position jointly within the EU. In the NEC framework, the position of Ukraine would be in sync with those of Georgia and Moldova and devoid of external influence by the EU to the extent that would be in the case of the CEFTA. The NEC establishment would serve to reinforce the economic ties of the AA signatory countries with each other and strengthen their positions in negotiations with the EU, since they would be able to speak up jointly within the EaP framework. At the fifth EaP Summit in Brussels on 24 November 2017, the EU did not support the 'EaP+' model, which had no systemic endorsement just on the part of the AA signatory countries.

At the second stage (the CES formation), there will be no need for the EU to scatter efforts on building separate integration models with each country. The recent uniting processes associated with the creation of the Western Balkans Regional Economic Area have proved that the EU still prefers group integration to individual integration. The rest of the EaP countries will be able to join

the NEC if they revise their attitude to the European integration policy. The CES NEC with the EU can be implemented in a form of either a customs union or common market, or else, eventually, as an economic union, i.e., de facto the accession to the EU.

The NEC establishment is the basic option. If its realization fails, it might be possible to resort to the CEFTA option in order to use the algorithms developed under the CEFTA for entering the EU common market.

The NEC establishment will mean orientation of the AA signatory countries to their further convergence with the EU. Therefore, bilateral FTAs as well as the CIS FTA will remain their economic relations' framework with the rest of the EaP countries, which will eventually require a revision. Preconditions for the revision in the short run are the deepened integration of Belarus and Armenia in the EAEU, and in the long run, the need for the NEC members to adopt the *acquis communautaire*. A separate study should be dedicated to a future Ukrainian-Belarusian economic cooperation model in view of the interlocking of the two economies.

At present, the three AA signatory countries continue declaring the full-fledged EU membership as their ultimate goal of cooperation with the EU. However, they express their current vision of economic integration development in different ways, so they need to come to a consolidated position among themselves. The main questions to agree upon include the depth of economic integration within the NEC, the NEC institutionalization, and the depth of economic integration of the NEC with the EU.

Yurii Vdovenko, PhD, Deputy Chairman of the Board at the Foreign Policy Council "Ukrainian Prism", member of the Steering Committee of the Eastern Partnership Civil Society Forum in 2016-2017. Graduated from Chernihiv National Technological University – Finance; and European Humanities University, the Center for Advanced Studies and Education (CASE) – Social Transformation in the Western Eurasia Border Region – Belarus, Moldova and Ukraine. Yurii has more than 90 scientific, analytical, and popular articles. His fields of interest are European integration, cross-border cooperation, local economic development, public-private partnership.
