

## **Policy Department External Policies**

# **THE COST/BENEFIT ANALYSIS OF THE ENP FOR THE EU'S EASTERN PARTNERS**

**FOREIGN AFFAIRS**

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## Executive summary

1. The Eastern neighbouring countries (NCs) can be divided into two groups: one comprised of the countries where ENP's benefits are (at least rhetorically) acknowledged (Georgia, Moldova, and Ukraine) and the other where the ENP is viewed with suspicion and where the Europeanisation drive is less palpable (Armenia and Azerbaijan, and, formally, Belarus as well).
2. In political terms, "a national consensus" exists in Georgia and Moldova on the need to Europeanise with all major parties supporting the respective bilateral Action Plans; in others (Ukraine), the rhetorical adherence to reform is undermined by strong political cleavages. Still, in other countries, authoritarian tendencies (Azerbaijan) or a preference of integration with Russia (Armenia) bar a real commitment to reforms.
3. In economic and social terms, the corner-stone of the ENP must be a substantial stake in the EU internal market. In the long run, establishing a "deep free trade area" is the only efficient way of convincing the relevant countries' economic elites that the ENP offers enough even for those constituencies whose businesses are currently heavily protected.
4. The public, while generally supportive of EU-related reforms, is badly informed and the Europeanisation process is either elite/bureaucracy-driven, or non-existent. Importantly, the priorities of key social groups differ in regard to the ENP. While for the political elites, frozen conflicts are often the key issue, business elites vie for better access to the EU market, and the population at large prioritises social stability and welfare.
5. Due to the absence of a membership perspective, NCs calculate the costs and benefits of complying with EU standards more critically than candidate countries. The key for enhancement is (1) to offer advanced neighbours association agreements which respond to different levels of ambition and offer a gradual approach of 'ever closer association'. Other improvements concern (2) the communicability of the ENP, (3) the streamlining of the numerous ENP offers around the establishment of a deep free trade area as well as capacity building for reform, and (4) the promotion of activities that have a visible impact on the everyday life of NC citizens.
6. The EU's overall approach of positive and case specific conditionality seems adequate. While political conditionality (value-based) is vaguely formulated, policy conditionality (acquis-based) shows a clearer relation between requests and rewards. In the framework of an association, the loose nexus between conditionality and compliance can be improved by establishing regular and fair monitoring and evaluation procedures including transparent benchmarks. In addition, the EU should further rely on direct and indirect effects of 'socialisation', e.g. through the inclusion of NCs in joint institutions and activities and through the diffusion of norms and paradigms as well as through financial and economic incentives.

## 1. POLITICAL COSTS AND BENEFITS, VESTED INTERESTS AND REFORM POTENTIAL

In regard to their attitudes toward the ENP-related reforms, Eastern ENP countries can be divided into two broad categories, one of which is comprised of those where political benefits of ENP-induced reforms are clearly acknowledged. In these countries, Europeanisation in general and ENP Action Plans in particular have become a major yardstick for domestic reform. Here, it is hardly possible to adopt any significant political measure without legitimising allusions to the EU. As a result, the European Union gains substantial leverage over the elites of these countries, and the benefits for compliance are considerable. The other group includes those countries where political elites have their doubts about the costs-benefits balance related to the ENP, and the Europeanisation drive is thus far less visible. The former category includes Ukraine, Georgia and Moldova, and the latter includes Armenia and Azerbaijan (and strictu sensu Belarus as well).

However, the rhetorical support for the policies listed in the Action Plan often does not correspond to real actions. In some cases, political elites would prefer “integration without Europeanisation”<sup>(1)</sup> and not integration through Europeanisation. This applies to a large degree to Ukraine, where a number of political actors take a wary stance toward the ENP (the former president Kuchma, economic groupings related to The Party of Regions, etc.). Similarly, in the Moldovan case, the legal approximation according to the Action Plan is not followed by implementation and independent enforcement by the judiciary. Unfortunately, this state is sometimes tacitly supported by the authorities.

For the countries in the second group, the ENP and eventual integration into the EU is, even if for different reasons, not seen as a priority. For instance, Azerbaijan with its authoritarian government (Aliyev’s New Azerbaijan Party) is rather wary in regard to any allusions to conditionality, and Azerbaijan’s “our-own-way” approach is further reinforced by the country’s rich natural resources. The Armenian elite is another example of a cautious approach to the ENP. For Armenia, the ENP does not offer a credible solution of the Nagorno-Karabakh conflict, and Russia remains Armenia’s key security anchor in the regional environment which Kocharian’s government still perceives as threatening. However beneficial the ENP can be economically, for the political elites in these countries, the ENP’s carrots are politically not conducive enough to make the ENP the centrepiece of their (domestic and foreign) policies.

The national assessment of the ENP’s merits is also closely related to national priorities and their reflection in the Action Plans. For a large majority of Eastern ENP countries (Armenia, Azerbaijan, Georgia, and Moldova), the political elites clearly see the resolution of the frozen conflicts on their territories as the single outstanding issue the EU should address. For instance, during the negotiations of the Action Plan, Moldovan Prime Minister Tarlev successfully demanded the inclusion of a special section dedicated to the Transnistrian Conflict. This was broadly publicised after his return and was interpreted as a substantial gain for Moldova<sup>(2)</sup>. To give a contrary example, Georgian authorities aimed to identify the frozen conflicts as priority number one but this was not reflected in the Action Plan which classes the issue among several other priorities. This failure, in connection with the EU-Russia visa facilitation agreement which applies to most inhabitants of Georgia’s separatist

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<sup>1</sup> Wolczuk, K., *Integration without Europeanisation: Ukraine and its Policy towards the European Union*, European University Institute, Florence, 2004. [http://www.eui.eu/RSCAS/WP-Texts/04\\_15.pdf](http://www.eui.eu/RSCAS/WP-Texts/04_15.pdf), consulted July 2007.

<sup>2</sup> Buşcaneanu, S., ‘How Far Is the European Neighbourhood Policy a Substantial Offer for Moldova?’, *Journal of Foreign Policy of Moldova*, No 9, EuroJournal.org, Chisinau, 2006. <http://www.e-democracy.md/files/enp-moldova.pdf>, consulted July 2007.

regions, substantially increased Georgia's scepticism in regard to the EU's ability to help solve the conflicts (<sup>3</sup>).

The final element crucial for the political cost/benefit calculations of virtually all Eastern ENP partners is the relation of the ENP's priorities to the dominant external actor in the region – the Russian Federation. Russia plays a substantial role in two different areas: First, at the domestic level, it is almost always the pro-Russian political forces in these countries that express the strongest reservations about reforms, in particular about those in the economic field as these reforms are often incompatible with the country's participation in the Russia-led Eurasian Economic Community or the Common Economic Space. Secondly, since Russia is directly or indirectly involved in all the frozen conflicts under discussion (Transnistria, Nagorno-Karabakh, South Ossetia, and Abkhazia), the political leaders of these countries closely follow the development of EU-Russian relations. Signs of a "Russia-first" approach (as in EU's past policies toward Southern Caucasus) are taken as signals that in spite of the allusions in the Action Plans, the EU's involvement in the conflict resolution is not serious enough. This is further strengthened by the fact that most new EU member states support the NCs in their critical assessment of Russia.<sup>4</sup>

#### Political elites and the ENP

Country	Attitude to ENP-related reforms	Impeding factors	Pro-reform constituencies	Opponents of reforms
Georgia	Consensual assent	Excessive focus on separatism, overambitious in relation to EU accession	All major political parties, e.g. The United National Movement	Marginal political groupings with pro-Russian orientation
Moldova	Consensual assent	Disinterested bureaucracy, insufficient implementation of adopted laws	All major political parties ("parliamentary consensus")	Transnistrian authorities
Ukraine	Rhetorical endorsement	Rhetorical adherence to reform, yet strong internal political cleavages	Our Ukraine	Parties with pro-Russian orientation and populists (The Communist Party of Ukraine, partially The Party of Regions)
Armenia	Cautious embrace	Russia-first approach	Heritage Party and several other small political groupings	Most parties, including the governing ones, prefer stronger ties to Russia
Azerbaijan	Cautious embrace	Authoritarian tendencies, self-assuredness based on oil, reluctance to accept conditionality	Opposition parties (e. g. Azerbaijan Popular Front Party)	The "party of power" (New Azerbaijan Party)

<sup>3</sup> Popescu, N., *Europe's Unrecognised Neighbours. The EU in Abkhazia and South Ossetia*, Centre for European Policy Studies, Brussels, 2007. [http://shop.ceps.be/downfree.php?item\\_id=1476](http://shop.ceps.be/downfree.php?item_id=1476), consulted July 2007.

<sup>4</sup> Kratochvíl, P., New EU Members and the ENP: Different Agendas, Different Strategies. In: *Intereconomics*. Vol. 42, No. 4, July/August 2007, pp. 191-196

## 2. ECONOMIC COSTS AND BENEFITS, VESTED INTERESTS AND REFORM POTENTIAL

The main element of any analysis of the economic costs and benefits of the ENP must be the assessment of the future free trade area (FTA) between the EU and the partner countries. Today, five central points must be taken into account:

1. An FTA will be clearly more beneficial for the Eastern neighbours than for the Southern ones, as tariffs are higher vis-à-vis Eastern Europe today than towards the Mediterranean (<sup>5</sup>).
2. The FTA should encompass not only duty-free trade in goods between the country and the EU, but it should also include far-reaching legislative harmonisation, liberalisation in agricultural trade and in services, and also a gradual liberalization of the movement of labour (more substantive visa facilitation agreements, lowering or entirely cancelling visa fees, etc.)
3. With the exception of the study on Ukraine, no detailed feasibility study on the impact of the FTA on the partner countries' economies has been released so far. However, several studies are being conducted and thus more light will be shed on the issue by the end of this year (<sup>6</sup>).
4. The impact of an FTA on the concerned economies will also depend on the (speed and scale of) trade reorientation toward the European Union. In addition, this is influenced by external factors such as Russian embargoes, which have caused a substantial speed-up of export restructuring in both Moldova and Georgia (in particular in regard to the wine industry).
5. The analysis of the impact of the FTA (or, for that matter, of the general economic consequences of the ENP) must be directly linked to the analysis of the political situation in the countries. In all of the NCs, strong connections between the political sphere and business interests exist and somewhere, the political and economic elites are almost identical (as for instance in Azerbaijan, but to a large extent in Ukraine and Moldova as well). In this sense, even though the FTA-arrangement is highly attractive because it is the only area where real integration could take place (a real "stake in the internal market" (<sup>7</sup>)), strong vested interests of parts of political elites might block its creation (as in the Ukrainian case – see below).

While a reduction or removal of tariffs alone would not substantially increase the NCs' economic growth, if it is linked to the successful implementation of other priorities specified in the Action Plan (rule of law, improvement of investment climate, reduction of corruption, decrease of discretionary power of state bureaucracy), the growth might reach double-digit figures (as predicted for Ukraine) (<sup>8</sup>). Countries which started with these reforms even prior to the adoption of the Action Plan, like Georgia, can show an extremely positive record of these

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<sup>5</sup> Economic Effects of Wider Europe, Conference of The Centre for European Policy Studies, 14 June 2004. [http://www.ceps.be/Article.php?article\\_id=358](http://www.ceps.be/Article.php?article_id=358), consulted July 2007.

<sup>6</sup> For the exception see Shumylo, O., *Ukraine and the European Neighbourhood Policy. Ensuring the Free Movement of Goods and Services*, Centre for European Policy Studies, Brussels, 2006. [http://shop.ceps.be/downfree.php?item\\_id=1315](http://shop.ceps.be/downfree.php?item_id=1315) and Shumylo, O. et al., *Free Trade between Ukraine and the EU: An Impact Assessment*, International Centre for Policy Studies, Kyiv, 2007. [http://www.pasos.org/content/download/10499/69123/file/FTA\\_Impact\\_E.pdf](http://www.pasos.org/content/download/10499/69123/file/FTA_Impact_E.pdf), consulted July 2007.

<sup>7</sup> *European Neighbourhood Policy: The Policy: Frequently Asked Questions*. [http://ec.europa.eu/world/enp/faq\\_en.htm](http://ec.europa.eu/world/enp/faq_en.htm)

<sup>8</sup> Trade Sustainability Impact Assessment of the Free Trade Area in the framework of the Enhanced Agreement between the EU and Ukraine, ECORYS, Rotterdam, 2007. [http://trade.ec.europa.eu/doclib/docs/2007/june/tradoc\\_135055.pdf](http://trade.ec.europa.eu/doclib/docs/2007/june/tradoc_135055.pdf), consulted July 2007.

reforms: Georgia has been labelled “the number one world reformer” by the World Bank (<sup>9</sup>), and in spite of the Russian embargo, its real GDP growth is forecast at almost 7 percent per annum for the next five-year period (<sup>10</sup>). Even more importantly, its rapidly improving administrative capacity and improved investment climate are reflected in the pour-in of foreign direct investments, which skyrocketed to 1,1 billion USD last year (<sup>11</sup>). Yet even for Georgia, which has covered a substantially longer path of reform than other Eastern neighbours, the outstanding reforms remain a painful burden. For instance, the criminal law reform alone, falling under the rule-of-law priority of the Action Plan, is estimated to cost 291 million GEL, i.e. almost 130 million euros, which amounts to around two percent of Georgia’s annual GDP (<sup>12</sup>).

It is vitally important that the EU succeed in drawing the separatist regions’ economies into the ENP’s framework as well. For instance, the introduction of the EU Border Assistance Mission on the border between (the Transnistrian part of) Moldova and Ukraine together with the offer for Transnistrian companies to register with Moldovan authorities to gain preferential access to the EU market has been working well – 270 Transnistrian companies were registered in Chisinau last year (<sup>13</sup>).

Generally, those who are blocking further economic liberalisation are the business and industrial groupings that have enjoyed special treatment from the state authorities and have succeeded in creating heavily protected markets for their products. In Ukraine, car and steel industries are the prime examples of such protection, and the leading entrepreneurs here employ the strategy of blocking deregulation efforts such as those listed in the Action Plan (transparency and predictability of the regulatory legislation, investment climate improvement, consultations with foreign investors, etc.) and sometimes even supporting new protectionist measures (such as a price ceiling for mineral resources used in metallurgy). The result is heavy costs for the society as a whole and for beginning entrepreneurs in particular as registering property and starting and closing businesses in Ukraine remain extremely complicated (<sup>14</sup>).

However, it should be noted that for most of these industrialists, the access to the internal market is very attractive as well. This applies in particular to Ukraine’s steel producers. On the whole, their hesitation to decide between further protectionist tendencies and opening-up to the EU depends (after Ukraine’s entry into the WTO) mainly on the guarantee of access to the internal market given by the Union.

Among the other costs of creating an FTA with the EU, two stand out for the NCs: Complying with the rules of origin (aimed against re-exports from third countries) and other technical requirements related to consumer and environmental protection, health standards, etc. The latter, i.e. non-tariff restrictions, will probably be the most costly (<sup>15</sup>). It is important to note that substantial financial means from the ENPI will have to be used in order to remove technical barriers of trade and bring about a sufficient level of harmonisation. Should the EU

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<sup>9</sup> Top 10 reformers. <http://www.doingbusiness.org/main/Top10Reformers.aspx>, consulted July 2007.

<sup>10</sup> New Rating A Positive Signal For Economic Outlook.

[http://www.fdi.net/bmi/bmidisplay.cfm?filename=OEMO\\_20070718\\_136095\\_xml.html](http://www.fdi.net/bmi/bmidisplay.cfm?filename=OEMO_20070718_136095_xml.html), consulted July 2007.

<sup>11</sup> Ibid.

<sup>12</sup> On Georgia’s GDP see World Economic Outlook Database.

<http://www.imf.org/external/pubs/ft/weo/2007/01/data/index.aspx>, consulted July 2007.

<sup>13</sup> Prohnychy, V. et al., *European Union – Republic of Moldova Action Plan: Assessment of progress in 1st Quarter of 2007*, EXPERT-GRUP and ADEPT, Kishinev, 2007. <http://www.e-democracy.md/files/euromonitor06en.pdf>, consulted July 2007.

<sup>14</sup> Economy Rankings – Europe and Central Asia.

<http://www.doingbusiness.org/EconomyRankings/?regionid=425>, consulted July 2007.

<sup>15</sup> Shumylo, O. et al., *Free Trade between Ukraine and the EU: An Impact Assessment*.

rely solely or predominantly on the countries' own resources, the motivation for reform would further decrease, hence rendering these countries less susceptible to advantages related to participation in the internal market (<sup>16</sup>).

#### Selected economic measures related to the ENP

Measure	Benefits	Costs	Pro-reform constituencies	Opponents of reform
FTA	Accelerated exports, GDP growth, higher budget revenues	Accession to WTO, law harmonisation, rules of origin, overcoming non-tariff barriers, decrease in exports to CIS, growth of public spending	EU-oriented exporters (e.g. iron ore producers in Ukraine, and recently also wine industry in Georgia and Moldova)	Business interests from protected industries (e.g. car industry in Ukraine), exporters to CIS
Removal of state aid, subsidies	Improved market efficiency	Rise in unemployment in non-competitive industries and regions, social instability	Pro-reform governments (Ukraine, Georgia), exporters keen to enter the WTO	Large, ineffective, often state-owned companies, heavily subsidized industries (e.g. machine-building in Ukraine)
Investment climate, improved transparency and predictability	FDI growth, faster economic growth	Administrative reform, judiciary reform, consultations with investors	Pro-reform governments (Georgia, Ukraine), external actors (IMF, EU)	Rigid bureaucracy, missing law implementation
Involvement of separatist regions	Poverty reduction, growth of trade with separatist regions	Political concessions to separatist authorities	Central governments (Moldova), external actors (EU, OSCE)	Central governments (Georgia), separatist authorities (Moldova), Russia

<sup>16</sup> For a more detailed discussion of this issue, see Shumylo, O., *Ukraine and the European Neighbourhood Policy. Ensuring the Free Movement of Goods and Services*.

### 3. SOCIAL COSTS AND BENEFITS, VESTED INTERESTS AND REFORM POTENTIAL

Although the societies of all Eastern partners are generally supportive of a deeper integration with the EU and vast majorities support the respective countries' EU accession (<sup>17</sup>), the level of knowledge about the EU is very low. For instance, it is clear from opinion polls that large parts of the society in Ukraine would favour a simultaneous integration into the EU *and* Russia, even though these two options are in many ways incompatible (<sup>18</sup>). Moreover, in all the analysed NCs, those parts of the population that are the most supportive of close economic and political ties with Russia (especially in Ukraine, Moldova, and Armenia) are the least in favour of the EU.

Because of the minimal knowledge of the EU, the societies in these countries remain largely indifferent to changes in governments' policies towards the EU as long as the general rhetoric of compliance with the EU and the agreed Action Plans do not change. In other words, the process of Europeanisation is almost exclusively elite-driven (Georgia, Moldova), and hence, it is in danger of disappearing once a new government comes to power. To a lesser degree, such a danger is present in Ukraine as well (where EU-inspired domestic reforms are predominantly bureaucracy-driven). Another potential risk lies in the fact that once the domestic situation deteriorates, political elites might use the Action Plan as a scapegoat which can be blamed for the country's problems, as frequently happened with membership candidates and Association Agreements during the preparations of the Eastern enlargement.

A further impeding factor is the divergence between the population and the political elites in regard to the perception of national priorities. Frozen conflicts in all NCs are stressed more by politicians than by the population at large. For instance, while Georgian politicians have been continually demanding the prioritisation of conflict resolution in the Action Plan, the population is more concerned with social problems such as poverty and unemployment (both considered significant problems by more than 90 percent of population) (<sup>19</sup>).

The economic situation of the population is very different in individual countries. In Ukraine, poverty has decreased to less than one fifth of the population (<sup>20</sup>), while in the Caucasian region, poverty remains an overwhelming problem and some poverty indicators even worsened in Moldova in 2005-2006 (<sup>21</sup>). Also, poverty is distributed unevenly in the countries, with the number of the poor rising in the rural areas, which is partially a consequence of Russian embargoes (vine growing in Moldova and Georgia) and sometimes even due to EU measures (Transnistria) as well.

Major benefits for the concerned societies would stem from reform steps listed under the "political reform" heading of the Action Plans. In all five NCs, violations of human rights are still frequent – for example, the Centre for Human Rights in Moldova registered a rising

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<sup>17</sup> Cf. Kratochvíl, P. (ed.), *The European Union and Its Neighbourhood. Policies, Problems and Priorities*. Institute of International Relations, Prague, 2006.

<sup>18</sup> Cf. Wolczuk, K., *Integration without Europeanisation: Ukraine and its Policy towards the European Union*. , European University Institute, Florence, 2004. [http://www.eui.eu/RSCAS/WP-Texts/04\\_15.pdf](http://www.eui.eu/RSCAS/WP-Texts/04_15.pdf)

<sup>19</sup> *European Neighbourhood Policy and Georgia*, Heinrich Böll Foundation, Open Society Georgia Foundation and Eurasia Foundation, 2007.

<sup>20</sup> Communication From the Commission to the Council and the European Parliament *On Strengthening the European Neighbourhood Policy*, Commission of the European Communities, Brussels, 2006. [http://ec.europa.eu/world/enp/pdf/sec06\\_1505-2\\_en.pdf](http://ec.europa.eu/world/enp/pdf/sec06_1505-2_en.pdf), consulted July 2007.

<sup>21</sup> Prohntichi, V. et al., *European Union – Republic of Moldova Action Plan: Assessment of progress in 3rd Quarter of 2006*, EXPERT-GRUP and ADEPT, Chisinau, 2006. <http://www.e-democracy.md/files/euromonitor04en.pdf>, consulted July 2007.

number of petitions in 2006 <sup>(22)</sup>, and harassment of political opponents and independent activists is common in Armenia and Azerbaijan as well.

Finally, the support for a civil society (communication strategy on environmental issues, involvement of civil society in educational programmes, etc.) is also vitally important. However, the support for networking among NGOs and their autonomy should be a priority goal since NGOs are fragmented and their financial support comes almost exclusively from abroad <sup>(23)</sup>.

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<sup>22</sup> Buşcaneanu, S., 'How Far Is the European Neighbourhood Policy a Substantial Offer for Moldova?'.  
<sup>23</sup> Cf. the situation in Moldova in Prohnychy, V. et al., *European Union – Republic of Moldova Action Plan: Assessment of progress in 2nd Quarter of 2006*, EXPERT-GRUP and ADEPT, Chisinau, 2006. <http://www.e-democracy.md/files/euromonitor03en.pdf>, consulted July 2007.

#### 4. INCENTIVES ENHANCING THE COST/BENEFIT BALANCE

In the absence of a membership perspective, NCs calculate the costs and benefits of complying with EU standards more soberly and discuss its implications more openly than the former candidate countries of Central and Eastern Europe (CEE). The problem with this otherwise rational attitude is that in the case of NCs, political momentum for 'Europeanisation' is weaker and that domestic reform elites must be more capable of writing the script that guides political and economic reform in their countries. The influence of the EU is thus decidedly more limited.

Two lessons learned from the pre-accession strategy for the CEE countries are relevant in this context. Firstly, the membership perspective mainly worked against the reversibility of the reform processes and solidified the formation of a democratic political mainstream. Secondly, the political and policy conditionality as enshrined in the Copenhagen criteria offered the candidates a comprehensive approach to simultaneously de-block the resistance to modernisation and reform in all relevant spheres of transformation. Reform paths in NCs will be comparatively inconsistent, patchy, and slow. With regard to both the irreversibility and the scope of reforms, the ENP offers less and is thus generally less attractive for the NCs. Notwithstanding these limitations, NCs regard the EU as the most engaged external actor who is vital for providing assistance for economic and political reform across the board and who also works as a focal point for activities of other organisations like the World Bank. However, there is room to improve the incentive structure of the ENP to enhance the cost/benefit balance for NCs.

*The first improvement concerns the nature of the relationship between the neighbours and the EU. The EU has the option to offer advanced neighbours an association and call them associates. Eastern NCs would highly appreciate this political gesture because they would no longer be discriminated against while Southern NCs enjoy association status. Moreover, it is a substantial offer because associations range from simple free trade agreements up to complex bi- and multilateral arrangements as is the case with Switzerland and the EEA respectively. The association framework thus responds to different levels of ambition and offers gradualism ('ever closer association'<sup>(24)</sup>) for successful reformers among the ENP countries.*

It is in the interest of the NCs that the envisaged agreements to succeed the PCAs should be legally binding and based on article 310 TEC (on establishing an association). In addition, they should be comprehensive in scope and foresee a durable arrangement with evolutionary potential, even if the agreements do not mention a finalité beyond the association<sup>(25)</sup>. NCs can hardly perceive offers below association as 'enhanced agreements'. As a reward for the reformer NCs (and from the EU's point of view as an element of conditionality), negotiations should only be opened if a sufficient level of political commitment and performance has been proven through implementing the Action Plan(s).

The established pattern of association is flexible enough to accommodate all sorts of highly intensified relations of cooperation and also integration between the EU and third countries. From the point of view of the NCs, association agreements are more concrete and

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<sup>24</sup> For a similar proposal dealing with a new type of association focusing on modernisation and stability see Lippert, B., Beefing up the ENP: Towards a Modernisation and Stability Partnership, *The International Spectator*, No. 4, Istituto Affari Internazionali, Rome, 2006, pp. 85-100; and Lippert, B., *EU – ENP and Russia – clash or cooperation in the triangle?*, Friedrich-Ebert-Stiftung, Fifth Roundtable Discussion, Berlin, 2007, pp. 12-35, here p. 30.

<sup>25</sup> Ukraine will certainly try to achieve a formula taking up its European aspirations in negotiations. Cf. *EU/Ukraine Action Plan*: '[T]he European Union acknowledges Ukraine's European aspirations and welcomes Ukraine's European choice.'

credible than any newly invented ‘Neighbourhood Agreements’, which would only be a second best option <sup>(26)</sup>. NCs can refer to current and historic examples of association and demonstrate that progress towards membership is not excluded. Given that negotiations are complex and ratification of the mixed agreements are a lengthy process, the NCs take an interest in highlighting the political and privileged character of the new association agreements that are worth these efforts. Moreover, they need to demonstrate some visible progress and advantages over the status quo (see below). For example, it would be important for the NCs to emphasise the upgraded role and competencies of the joint institutions in the association framework. In particular, the right of the joint association council to make binding decisions for the development and substance of the bilateral relations is really progressive and should be communicated in this way.

Depending on the domestic constellations of pro-reform elites and their opponents in NCs, the multi-level institutional structure of the association is regarded as an avenue to constantly get more and better qualified actors involved in ‘Europeanisation’ processes through direct interaction with EU actors. Apart from the high ranks of the executive, the ministerial bureaucracy in line ministries (and probably also members of parliaments) can be addressed as domestic stakeholders of reforms that oversee implementation of domestic reforms and action plans <sup>(27)</sup>.

*The second* improvement concerns the *communicability* of the ‘ENP’. For an NC, to become an associate is far more attractive and meaningful than simply being called a neighbour. This would also help to reduce mixed messages about the political finalité of the relations currently reflected in a variety of formulations used to grasp the nature of the relationship like ‘privileged’ or ‘strengthened relationships’, ‘privileged reform relationships’ etc. <sup>(28)</sup>. Moreover, the EU should be open to proposals of NCs to formulate the focus and *leitbild* of their specific relations in a way that can be better communicated to domestic stakeholders of reform in the political parties, the business community, the media and among citizens. Everything that makes the EU more visible as a reform partner who takes due account of country specifics is seen as an advantage. NCs value the principle of differentiation and room for a multi-speed development in the ENP area. From the NCs’ perspective, the term ENP should rather be used as a technical term for EU internal purposes which apparently needs a single framework for its tailor made policies vis-à-vis the 16 neighbours.

*The third* improvement concerns a *streamlining* of the numerous offers. This would help the NCs join and direct domestic forces towards key targets and increase the awareness of joint ownership. Given the rich and crowded menu of actions listed in the EU’s strategy papers, national indicative programmes or the Action Plans, NCs often miss a red thread for

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<sup>26</sup> Speech of Roman Shpek, Representative of Ukraine to the EU at the Study Day of the EPP-ED Group on Ukraine, 8 December 2005, Brussels. <http://www.ukraine-eu.mfa.gov.ua/eu/en/publication/content/4896.htm>, consulted August 2007; Speech of the Moldovan President Vladimir Voronin in front of the members of the Committee on Foreign Affairs of the European Parliament, 8 June 2005, Strasbourg. [http://www.europarl.europa.eu/meetdocs/2004\\_2009/documents/fd/dmd20050621\\_08/dmd20050621\\_08en.pdf](http://www.europarl.europa.eu/meetdocs/2004_2009/documents/fd/dmd20050621_08/dmd20050621_08en.pdf), consulted August 2007.

<sup>27</sup> Cf. Wolczuk, K., *Adjectival Europeanisation? The Impact of EU Conditionality on Ukraine under the European Neighbourhood Policy*, European Research Working Paper Series No. 18, European Research Institute, Birmingham, 2007. [http://www.eri.bham.ac.uk/research/working\\_papers/WP18Wolczuk.pdf](http://www.eri.bham.ac.uk/research/working_papers/WP18Wolczuk.pdf), consulted August 2007. Cf. below on the importance of socialisation effects.

<sup>28</sup> Communication From the Commission *European Neighbourhood Strategy Paper*, Commission of the European Communities, Brussels, 2004, p. 3; Communication From the Commission to the Council and the European Parliament *On Strengthening the European Neighbourhood Policy*, Commission of the European Communities, Brussels, 2006, p. 2; Note from the General Secretariat to the Council *Strengthening the European Neighbourhood Policy – Presidency Progress Report*, Council of the European Union, Brussels, 2007, p. 3.

reform. In the absence of a catch-all-solution, i.e. the complete take-over of the *acquis* of the EU, the cognitive and practical capacities of the NCs to draw up their reform programmes need strengthening. Extra time and concrete assistance (via Twinning including parliamentary twinning, TAIEX, independent experts, political parties and parliamentarians) must be provided by the EU and member states to support domestic elites to elaborate priorities and plan the sequencing of measures that should make up the national reform plans and be reflected in the Action Plans or equivalent plans. Even if association agreements enter into force, there is need for some type of work programme for reforms that allows for a successful packaging of measures instead of isolated activities attained with more difficulty. Also, a new term has to be invented for this plan once the new stage of relations is achieved.

The establishment of a deep and comprehensive free trade area is the biggest economic carrot which the EU offers. Improved and asymmetrical market access for sensitive goods, e.g. agricultural, food and chemical products, metallurgy or textiles, is crucial for NCs. In practical and psychological terms, it is a test case of the EU's credibility in enhancing its relations with NCs. A more demanding step for the NCs is the adoption of regulatory reforms that are essential for making use of the deep free trade area. The EU can support convergence with the regulatory sector in several ways, e.g. through knowledge transfer and the opening of relevant agencies and programmes for NCs as well as through directing its financial assistance towards these ends<sup>(29)</sup>. A real boost in this regard can be expected from the attraction of FDI. The inflow of FDI will be the major engine for modernisation as was the case in the early and mid 1990s in the CEE candidate countries. Complying with EU rules and standards is certainly conducive to attracting foreign investors. However, in the first place, a far more transparent business environment, level commercial playing fields and legal certainty must be achieved in the NCs. Hence, progress in good governance is decisive. The crucial problems are overly complicated taxation systems and high levels of corruption within large informal sectors<sup>(30)</sup>. With the help of the EU, the reformist elites in NCs could focus their reform activities on these and other related issues.

Among other sectors, progressive access to the internal energy market of the EU is attractive for NCs like Moldova, Armenia, Ukraine, and Georgia<sup>(31)</sup>. In this respect, the EU could use the instrument of sectoral agreements or amendments to the association agreements. Most NC elites are not yet prepared to live with what unfortunately looks like an 'untidy' web of agreements that merely follows a functional approach of cooperation and a significant degree of integration (e.g. 'energy community' or 'transport community'). Therefore, it is also in the interest of the NCs to increase synergy between co-existing activities, arrangements, and agreements in order to make them more efficient.

Also, NCs have mixed feelings about boosting regional cooperation. However, it could be interesting for the NCs to further explore the potential of regional cooperation between the EU, NCs and candidate countries. The degree of interest in a 'multilateral umbrella' varies significantly, and the overriding interest is in bilateral relations with the EU. Therefore, the idea of a 'Neighbourhood economic community' might be premature or even discouraging for frontrunners<sup>(32)</sup>. Practical sectoral results might be more powerful arguments than the

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<sup>29</sup> Solonenko, I., *The EU's 'transformative power' beyond enlargement: the case of Ukraine's democratisation*, European Research Working Paper Series No. 21, European Research Institute, Birmingham, 2007. [http://www.eri.bham.ac.uk/research/working\\_papers/WP21Solonenko.pdf](http://www.eri.bham.ac.uk/research/working_papers/WP21Solonenko.pdf), consulted August 2007.

<sup>30</sup> Cf. Milcher, S., Slay, B. and Collins M., 'The Economic Rationale of the "European Neighbourhood Policy"', In: Ålsund, A. (ed.), *Europe after Enlargement*, Cambridge University Press, Cambridge, 2007, pp. 165-188, here p. 177.

<sup>31</sup> *Ibid.*, pp. 179-181.

<sup>32</sup> Communication From the Commission to the Council and the European Parliament *On Strengthening the European Neighbourhood Policy*, Commission of the European Communities, Brussels, 2006; Lippert, B., 'The

elaboration of master plans to construct a single overarching structure to accommodate all aspects and areas of interaction between the EU and the NC(s).

For the most reform-minded NCs, a strengthening of the foreign policy aspects of ENP is attractive: Moldova and Georgia would certainly welcome a stronger engagement of the EU in the resolution of frozen conflicts. Given that political dialogue is a core element of association, the NCs expect that the EU will address these problems more pro-actively in their bilateral relations and also in their relations with Russia<sup>(33)</sup>. Conflict reduction and resolution and the building of a stable external environment are often regarded as a pre-condition for the internal democratisation and improvement of responsiveness and the strengthening of the resonance of the ruling elites towards EU conditionality<sup>(34)</sup>.

*The fourth* improvement is to promote activities that have a significant and visible *impact on everyday life* in NCs. Of major interest are activities related to the movement of people like visa facilitation, exchange programmes (including those that are not explicitly for young students), and smooth border management. As visa facilitation is strictly dependent upon the conclusion of readmission agreements, the EU should increase its technical and financial support to help the NCs to fulfil their anti-trafficking obligations. Additionally, the consular services of some member states need serious improvements which would reduce bureaucratic complications when NC citizens try to apply for visas. Recognising this drawback, the Commission has already proposed the establishment of common visa-application centres<sup>(35)</sup>. Possibilities of multi-entry visas and a reduction of prices should be further considered, in particular after new member states will have joined the Schengen zone which crucially affects Poland's direct neighbours Belarus and Ukraine, for example. Aside from that, the everyday life of NC citizens would also be affected by visible progress in environmental protection and in combating disease epidemics like HIV/AIDS<sup>(36)</sup>.

In general, the identification of one or two *joint projects* with the EU could enhance the focus and support of ENP activities in the NCs. In the field of transportation, for instance, a further extension of the pan-European corridors into the NCs would be of immediate benefit to these countries and will, in the longer run, catalyse deeper economic integration. However, since bottlenecks along those corridors are often policy-induced, e.g. by time-consuming and corruption-prone border control procedures, infrastructure funding needs to be complemented by capacity-building measures<sup>(37)</sup>.

While these improvements, which mix policy incentives for economic and political reforms and practical advantages, mostly reflect the interests of reform minded NCs, it is clear that the NCs that have other policy choices or want to avoid the political costs will not grasp the new opportunities and incentives.

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EU-Neighbourhood Policy – Profile, Potential, Perspective', *Intereconomics: Review of European Economic Policy*, No. 4, Springer-Verlag, Heidelberg, 2007, pp. 180-187.

<sup>33</sup> Cf. Lippert, B., *EU – ENP and Russia – clash or cooperation in the triangle?*, Friedrich-Ebert-Stiftung, Fifth Roundtable Discussion, Berlin, 2007, pp. 12-35.

<sup>34</sup> Cf. Czempiel, E., 'Demokratisierung von außen. Vorhaben und Folgen', *Merkur*, No 6, Klett-Cotta, Stuttgart, 2004, pp. 467-479.

<sup>35</sup> Emerson, M., Noutcheva, G. and Popescu, N., 'European Neighbourhood Policy Two Years on: Time indeed for an 'ENP plus'', *CEPS Policy Brief*, No 126, Centre for European Policy Studies, Brussels, 2007, pp. 18-19.

<sup>36</sup> Milcher, S., Slay, B. and Collins M., 'The Economic Rationale of the "European Neighbourhood Policy"', pp. 181-184.

<sup>37</sup> Cf. Emerson, M. et al., *The Prospect of Deep Free Trade between the European Union and Ukraine*, Centre for European Policy Studies, Brussels, 2006, pp. 91-92.

## 5. CONDITIONALITY - ITS ADEQUACY AND POTENTIAL ALTERNATIVES

*Where does conditionality occur?* Conditionality defines a relationship between the EU and NCs in which the EU offers rewards under the condition that the NC adopts democratic rules and practices and fulfils the other requirements of the EU. In the ENP context, it is a positive conditionality that is mostly applied and referred to in respective documents. It concerns political (value-based) as well as policy (acquis-based) conditionality. Political conditionality is rather vaguely formulated in ENP documents, considerably toning down the requirements and combining them with uncertain rewards<sup>(38)</sup>. Policy conditionality shows a somewhat clearer relation between request and reward. For example, the fulfilment of the Action plan objectives leads to the opening of negotiations on an enhanced agreement<sup>(39)</sup>; WTO membership is seen as a precondition for the establishment of a free trade agreement<sup>(40)</sup>; regulatory approximation is a precondition for deep free trade<sup>(41)</sup>; progress on readmission and border management leads to the opening of negotiations on a visa facilitation agreement<sup>(42)</sup>. Examples of policy conditionality show that the EU mainly wants to encourage progress through incentives which are sometimes concrete (such as granting Autonomous Trade Preferences or opening up certain Community agencies and programmes to the NCs) or in other cases remain vague (such as the *prospect* of further consultations on visa facilitation or deeper economic relations).

Negative conditionality, which means a loss of support and assistance in case an NC does not comply, is only foreseen in the context of the ENPI when granting funds<sup>(43)</sup>. The ENP framework does not provide for additional punitive measures.

*How does it work?* However, political leverage of the EU depends on the existence and the range of policy choices an NC has in dealing with the EU. So far, the EU has exercised a loose nexus between conditionality and compliance. Neither ‘strict conditionality’ with a clear relationship between compliance and membership nor a new ‘light’ catalogue of criteria (‘Copenhagen light’) is introduced. Benchmarks exist but key EU actors like the Commission, the Council and the EP have not spelled them out in a transparent way. Apart from conditionality, the EU relies on direct and indirect effects of ‘socialisation’, e.g. through inclusion of NCs in programmes and agencies and possibly also in other EU institutions<sup>(44)</sup> or in joint institutions under the enhanced/association agreements as well as in joint activities in the future through the diffusion of norms (such as the Copenhagen criteria)<sup>(45)</sup> and paradigms (such as regional cooperation; social cohesion etc.) and also through financial and economic incentives. The EU tries to initiate competition between NCs through rewarding

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<sup>38</sup> A good example of this is the following statement: ‘The level of ambition of the EU’s relationships with its neighbours will take into account the extent to which these values are effectively shared’ (Communication from the Commission *European Neighbourhood Strategy Paper*, Commission of the European Communities, Brussels, 2004, p. 3.)

<sup>39</sup> *EU/Georgia Action Plan*, p. 4.

<sup>40</sup> Note from the General Secretariat to the Council *Strengthening the European Neighbourhood Policy – Presidency Progress Report*, Council of the European Union, Brussels, 2007, p. 8.

<sup>41</sup> *Ibid.*, p. 7.

<sup>42</sup> *EU/Ukraine Action Plan*, p. 30.

<sup>43</sup> *Regulation (EC) No 1638/2006 of the European Parliament and of the Council of 24 October 2006 laying down general provisions establishing a European Neighbourhood and Partnership Instrument*, Article 28: ‘[W]here a partner country fails to observe the principles [of liberty, democracy, human and fundamental rights], the Council, acting by a qualified majority on a proposal from the Commission, may take appropriate steps in respect of any Community assistance granted to the partner country under this Regulation.’

<sup>44</sup> Cf. The procedures established for structured dialogue with the candidates from CEE or the special institutional arrangements of the EEA.

<sup>45</sup> Cf. Yushchenko, V., ‘Angriff auf die Demokratie’, *Frankfurter Allgemeine Zeitung*, 19 June 2007.

advanced performers. A concrete example is the governance facility fund. Its management and allocation principles can be an important signal for NCs also with regard to credibility of conditionality (<sup>46</sup>).

*Is it adequate?* One weakness of the EU's approach is the credibility of conditionality. In the absence of a punishment option, the EU's negative conditionality is a blunt instrument. While positive conditionality has its limits as well (no membership incentive), there exist rewards below membership (see above). Here, one limitation is that the EU does not want to raise overly high expectations (e.g. the establishment of a gradual road map with clearly defined stages that lead up to the opening of membership negotiations equivalent to the one for the Western Balkan countries). The EU is concerned about the problems of automaticity. Size of rewards is a constant problem because the EU cannot sufficiently compensate hard domestic reforms. The EU must, however, be aware of the balance between 'give and take' that differs from one NC to another. Besides the size of rewards, the timing of rewards is also crucial. By delivering its rewards gradually over time the EU could tackle the problem of 'time inconsistency' (<sup>47</sup>), which means that countries are less willing to reform when costs are expected in the short run whereas the benefits occur only in the long run. That is why asymmetry (e.g. in the opening of markets) and also symbolic policy are important elements of the ENP.

Another weakness is that conditionality is inconsistent because the EU needs to balance the different interests it pursues in relation with the NCs. Where overriding security and other foreign policy interests exist, the EU is less concerned and strict about political conditionality. This is the case with Azerbaijan, which, as a resource-rich country, is of special geostrategic importance for the EU (<sup>48</sup>).

*Can it be improved?* Mechanisms to monitor and evaluate conditionality are more elaborate, transparent and probably fairer in the framework of an association, in particular if it is a substantive/deep one as envisaged with Ukraine. The two parties can lay down detailed and clear procedures (including those of suspension and other sanctions) in cases of conflict and non-compliance within a binding legal framework.

It is in the interest of NC governments that the Commission will issue annual progress reports, starting in April 2008. Some NC governments, like the Ukraine, have already signalled to the Commission that regular evaluations of their performance would be helpful in order to increase pressure on domestic actors. Reports could preferably focus on the overall state of reforms in each NC with a special eye on ENP action plans. In addition the Commission could elaborate other tools like an 'ENP regulatory handbook' (<sup>49</sup>). Beforehand, the EU has to decide on a case-by-case basis how far and deep it wants to get locked into the domestic processes of transformation and reform of an NC and what the strategic and political implications for the EU would be.

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<sup>46</sup> Communication From the Commission to the Council and the European Parliament *On Strengthening the European Neighbourhood Policy*, Commission of the European Communities, Brussels, 2006, p. 12: 'An amount of €300m (some €43m per year, on average) for a Governance Facility, intended to provide additional support, on top of the normal country allocations, to acknowledge and support the work of those partner countries who have made most progress in implementing the agreed reform agenda set out in their Action Plan.'

<sup>47</sup> Cf. Tocci, N., Does the ENP Respond to the EU's Post-Enlargement Challenges?, *The International Spectator*, No.1, Istituto Affari Internazionali, Rome, 2005, pp. 21-32, here p. 32.

<sup>48</sup> Azer B., *Strategie und Demokratie. Azerbajdžan und die EU-Nachbarschaftspolitik*, Osteuropa, 57, 2-3, 2007, pp. 201-208.

<sup>49</sup> Emerson, M., Noutcheva, G. and Popescu, N., 'European Neighbourhood Policy Two Years on: Time indeed for an 'ENP plus'', *CEPS Policy Brief*, No 126, Centre for European Policy Studies, Brussels, 2007. [http://shop.ceps.be/download.php?item\\_id=1479](http://shop.ceps.be/download.php?item_id=1479), consulted August 2007, p. 16.

Overall, as far as policy conditionality is concerned, a clearer incentive structure linking demands and offers – including timetables for implementation and other benchmarks - and corresponding reform priorities of the NCs can be achieved. Political conditionality will, however, remain weak and effects of ‘socialisation’ and ‘passive leverage’ (i.e. the impact that the EU has on domestic policy choices of candidate and neighbouring countries by its mere existence and attraction)<sup>(50)</sup> are more important at the present stage. Given the current principles of the ENP <sup>(51)</sup> and the capacities of the NCs, the EU’s overall approach in giving priority to constructive, positive and case specific conditionality over overly ambitious criteria and absolute benchmarks (as in the case of the Copenhagen criteria) seems adequate.

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<sup>50</sup> Cf. Vachudova, M., *Europe Undivided. Democracy, Leverage, and Integration since 1989*, Oxford, 2005.

<sup>51</sup> General Affairs and External Relations Council, *Draft Council Conclusion on Strengthening the European Neighbourhood Policy*, 18/19 June 2007.

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