Economic Development and Security in the Black Sea Region

Report by the CSIS New European Democracies Project

About the Project

At a recent international conference in Washington, D.C. entitled Economic Development and Security in the Black Sea Region the New European Democracies Project at the Center for Strategic and International Studies (CSIS) assembled a prominent group of experts to examine economic and security issues affecting the Black Sea region. The Romanian Chamber of Commerce and Industry (CCIR) and General Dynamics sponsored the project, which provided a forum for participants to assess how regional cooperation among the Black Sea states can be increased through political, economic, and security instruments in the years ahead.

In addition, the conference examined U.S. and EU assistance in helping to meet the challenges the region now faces and considered proposals for enhancing this assistance. The implications for U.S. basing, energy security, the future of Europe’s Neighborhood Policy (ENP), and relations with Russia received special attention.

According to Janusz Bugajski, director of the New European Democracies Project at CSIS, “The conference helped to lay the foundations for a productive dialogue on the future of the Black Sea region. It is clear that Romania will play a key role in shaping both the NATO and EU approach to Europe’s ‘newest frontier.’”

Since the end of the Cold War, the Black Sea region has no longer been a static border between the West and the East. The disintegration of the Soviet Union radically increased the number of independent players around the basin and brought new political, economic, and social forces to the region. Despite such important transformations, however, Western institutions focused primarily on the transition of Central and Eastern Europe and did not view the Black Sea region as a distinct zone. For about a decade after 1989, the Black Sea area largely remained outside the reform and integration agenda of the European project. Today, the Black Sea region is reemerging from the periphery and establishing itself as a part of the Euroatlantic project.

In sum, the Black Sea basin is a strategically important region at the crossroads between Europe, the Middle East, and Asia. The region serves as a pivotal East-West and North-South corridor and a crossroad of geopolitics, commerce, energy, and culture where the interests of four major international actors overlap: the European Union (EU), the United States (U.S.), NATO, and Russia. It is a very dynamic area that presents various challenges and offers numerous opportunities. As a result, its development requires special consideration by policy makers.
The Need for Regional Approach

Although the Black Sea region has succeeded to attract the focus of regional actors and major international players in the last few years, there are lingering misconceptions that need to be addressed. Countries and organizations often approach Black Sea issues from specific national interests or on a bilateral basis. What is missing is a strategic vision of the region as a whole and a more comprehensive strategy for its development. The area needs a common agenda that should transcend the self-interests of local actors.

The challenges that the Black Sea region faces are interrelated but can be classified into four major components:

- Democratization and reform
- Economic development
- Security
- Euroatlantic integration.

On the other hand, there are various actors that interact in the Black Sea arena. They can be divided into three groups of diverse interests that are sometimes conflictive:

- Russia and Turkey
- The smaller Black Sea countries – Bulgaria, Georgia, Moldova, Romania, and Ukraine.
- The EU, the United States (U.S.), and NATO

Russia and Turkey are historically former status quo powers in the Black Sea region, with greater aspirations for regional leadership. The other, smaller littoral states are heterogeneous actors with distinct national agendas. While Bulgaria and Romania have become EU and NATO members, Georgia, Moldova, and Ukraine are intent on conducting reforms that can move them closer to the Euroatlantic structures. Meanwhile, the EU, the U.S. and NATO may have common interests and objectives in the region but do not always share joint policies and approaches.

Dialogue, cooperation, and consensus are difficult to achieve among the various players. Many of the newly independent states are pursuing distinct national interests, a process that often hinders conceptualizing the region as a common space. Meanwhile, Russia is intent on regaining influence over its former Black Sea dominions and preventing the region from integrating into the Euro-Atlantic structures.

In this context, the goal of the CSIS Black Sea forum was to address two key regional issues – economic development and security – and to offer specific policy recommendations that can be incorporated into a more comprehensive strategy for the area.

PANEL I – BLACK SEA ECONOMIC DEVELOPMENT

In recent years, economic development in the region has been relatively encouraging. The picture is especially positive with regard to Bulgaria, Romania, and Turkey. These three countries are not only economic leaders in the Black Sea region, but also among the fastest growing economies. Following severe economic crises in the late 1990s and early 2000s, each country has conducted intense structural reforms resulting in rapid economic
development and political stability. In the case of Bulgaria and Romania, important roles have been played by the International Monetary Fund (IMF) and the EU, which have provided guidance for reform and sound economic policies. This has brought economic stability and unlike the past decade, reforms are not cyclical but consistent. The main pillar of economic transformation and growth has been privatization and restricting state control. As a result, Foreign Direct Investment (FDI) is increasing each year and the Black Sea countries register annual economic growth of between 5 and 8 percent.

Despite general positive trends, economic development still remains below satisfactory levels and the pace differs between each country. There are several serious concerns at the state level that are valid for all countries and are problematic for the region’s development as a whole. Most importantly, barriers to market access include weakness in the rule of law, corruption, excessive bureaucracy, and ineffective judicial systems. All these factors limit the ability of local entrepreneurs and foreign investors to do business.

**Economic Challenges**

**Rule of law**
This is the most significant restriction on economic development that affects indirectly all other factors. Much effort has been expended by governments to advance the rule of law with legislation constantly adopted or modified. However, the speed of economic reform has exposed the limited capacity of the judiciary and the administration to adjust and apply the new laws. On paper, legislation looks effective but implementation and enforcement is often weak, as is the case with the protection of intellectual property. Countries such as Bulgaria and Romania have experienced rapid development in IT and high tech industries, but have a poor record on the protection of intellectual property.

The statistics on FDI show that there has been a large flow of international capital into the Black Sea region. In addition to a relatively cheap labor force and an educated population, the area is attractive to investors because it is a good launching point for new markets. Clearly the region is opening up. However, in order to continue this trend, effective rule of law is needed to secure trust and create a friendly environment for investors.

**Corruption**
The fact that even Bulgaria and Romania, which are regional economic leaders and new EU member states, are frequently criticized for corruption by the EU indicates the widespread problem in the Black Sea region. High levels of corruption in public administration and the judiciary remain a primary concern for businesses seeking a fair and predictable economic climate.

**Politics**
An eye must also be kept on populist and nationalist trends in Black Sea countries and how these may impact on the continuity of economic reform, the pace of development, and the degree of openness to foreign investment.

**Balance of Payments**
The current account deficits of all Black Sea countries are growing, which might affect their economies in the long term. The collapse of the Soviet Union resulted in the loss of state-mandated markets for the states in the region and led to a decrease in exports and upsurge in imports. To offset
this trend, local industries will have to improve their efficiency and competitiveness in order to reduce the growing trade deficits in all Black Sea countries.

**Agriculture Dependent Economies**
The Black Sea countries have large rural populations and agriculture remains a significant fraction of their GDP. This makes the economy dependent on rural development and may hinder economic growth.

These domestic concerns are fundamental for the economic development of all Black Sea states and the region as a whole. In addition, there are other, more complex issues that transcend national borders:

**Free Trade Agreements**
Regional cooperation in trade is often impeded by protectionist national policies. Trade relations between Black Sea countries are conducted mostly on an ad hoc bilateral basis. Bulgaria and Romania are the only signatories to the expanded Central European Free Trade Agreement (CEFTA). There is a strong need to promote free trade agreements and to facilitate cooperation, which would boost all economies in the region.

**Energy**
The Black Sea economies are heavily dependent on Russian gas and oil. In the last decade, Moscow has lost its status as a military superpower and has chosen to reestablish its influence largely through economic means and energy supplies. As a result, the region is penetrated by Russian capital that provides Moscow with political leverage and fosters dependency rather than development and economic growth. Hence, countries in the region remain economically vulnerable to Russia as an “energy superpower.” Under these circumstances, attempts to secure full political independence from Moscow may result in damages to national economies as Russia can impose economic sanctions.

Energy diversification is a major challenge in the region. Finding new routes for the transportation of Caspian oil through the Black Sea area will help the region develop economically, while decreasing Europe’s dependence on Russian energy. Two elements are crucial. First, financial support and investments are needed for specific projects and to develop energy infrastructure. Second, time is of paramount importance for the success of these projects. While European companies are slow in constructing alternative pipelines from the Caspian basin, President Vladimir Putin has indicated that Russia will launch new pipeline projects that could make some Western initiatives obsolete.

**Infrastructure**
It is paradoxical that Europe needs more energy, but has shown insufficient readiness to exploit the energy resources of the Black Sea region or to improve the region’s energy and transportation infrastructure. Exploiting natural resources will necessitate the development of the region’s roads, railroads, pipelines, and communication systems because they are old and inadequate for future needs. The modernization of infrastructure is also crucial for economic development. The demand for FDI is enormous. However, there is some deadlock, in that FDI is needed for the development of infrastructure, but investors keep out due to poor infrastructure. This would be easier to overcome with the prospect of EU membership and the granting of pre-accession funds for the Black Sea countries.

Successful transformation in the region depends on both political and economic progress. Effective political reforms without economic transformation can weaken public trust in democracy and fuel social and ethnic tensions. This would undermine development and challenge the region’s stability.
Policy Recommendations: Economic Issues

1. Financial Support and FDI: International investors are crucial for continued economic growth in the Black Sea region. Providing economic and tax incentives may be insufficient. In order to create a suitable environment and attract substantial amounts of FDI, the region’s governments must guarantee the rule of law, effectively tackle corruption, and reform the judiciary system. This would bring a sense of security for foreign banks and companies.

2. Privatization: Removing the state from the economy and enabling private business is key to sustained economic growth and for attracting FDI. Privatization should be supported and facilitated by governments in the Black Sea region, especially in countries that still hold a substantial sector of industries in state hands.

3. Development of Banking and Financial Sector: Experience in Bulgaria and Romania indicates that sustainable economic growth is only possible after the banking system has been restructured and privatized. Western banks introduce new standards in crediting and operations, which stimulates production and consumption. Three main factors enable the development of the banking sector: political will to restructure the economy; foreign companies applying pressure on the system to be restructured; and political support of the EU for European banks to enter the Black Sea market. Both national governments and the international community should cooperate to open up the Black Sea banking sector and to help generate more substantial FDI in the area.

3. Free Trade: Littoral states should take advantage of geographic proximity and transport corridors in the Black Sea. Governments should be more flexible in facilitating cooperation and working toward creating a free trade area that would boost regional economic performance. In this context, accession to the World Trade Organization (WTO) is an important step for all Black Sea countries. The littoral states should set their priorities more clearly and perhaps reevaluate their membership in the Russian-dominated Commonwealth of Independent States (CIS).

4. Infrastructure: The modernization and advancement of infrastructure is a precondition for substantial economic growth. Black Sea governments should give special priority to infrastructure and mobilize large-scale investments from both local and international players.

5. Energy: The prospects for energy independence or non-dependence in the Black Sea region are somewhat remote. As a result, each capital must adjust to these circumstances and adopt flexible and effective approaches toward Russia in order to secure their immediate energy needs and prevent any negative effects on the economy. This would also enable the drive for diversification. Governments need to explore the development of alternative energy sources such as electric, thermal, wind, and hydro. Some Black Sea states such as Bulgaria, Romania, and Turkey seek expanded nuclear energy programs to promote flexibility. Black Sea capitals must also allocate sizeable investments in the modernization of infrastructure that would enhance regional cooperation in securing alternative energy routes from the Caspian Basin.

6. Regional Cooperation: Regional development projects in infrastructure are crucial. However, even if they have financial backing from international institutions, they cannot become reality without more intensive cooperation between the Black Sea countries. Small bilateral or regional projects are extremely important for building relations. The private sector needs to take the initiative to lay the foundations for such cooperation. Strategic partnership with Russia should also be developed in a way that fosters economic development rather than creating obstacles and dependency.
PANEL II – BLACK SEA SECURITY ISSUES

After September 11, 2001, the strategic importance of the Black Sea territory was further reinforced. The U.S. led war against terrorist groups and the NATO action plan against terrorism defined a specific role for the region in its new security dimension. Nevertheless, Black Sea security cannot be perceived only in the sense of transatlantic security. The region confronts a wide array of challenges that undermine its stability, including unresolved secessionist conflicts, Russian military threats, weak states, large-scale international organized crime, and the presence of terrorist groupings.

Security Challenges

Frozen Conflicts

“Frozen conflicts” are the primary source of instability and the largest security threat in the region. Georgia, Moldova, Armenia, and Azerbaijan cannot progress toward the Euroatlantic structures without resolving the separatist conflicts within their borders that challenge territorial integrity and political stability. These conflicts also threaten economic integrity and performance; for example, forty percent of Moldova’s industry is located in Transnistria.

For unstable transitional states, the “frozen conflicts” also maintain tensions with Russia as Moscow seeks to benefit from the ongoing conflict. The presence of Russian troops in Moldova and Georgia represents a significant security risk for both states, which fear partition and annexation by the Russian Federation. The “frozen conflicts” threaten state integrity and pose a security threat to the broader region. The secessionist entities are undemocratic satellites with regimes involved in trans-national criminal activities such as trafficking.

Maritime Domain and Border Security

As an important crossroad of commerce, the Black Sea region offers numerous opportunities for regional cooperation. However, its location also facilitates illicit trade in migrants, arms, and drugs. Such threats should not be underestimated as they fuel political and terrorist movements and disrupt regional economies. With Bulgaria and Romania becoming the external boundary of the EU, border security in the Black Sea area is becoming extremely significant for Europe as a whole.

Euroatlantic Prospects

NATO Action Plans have had a positive impact in the Black Sea region. However, Russia as an energy superpower is becoming more assertive, more authoritarian, more competitive, and less cooperative. Non-NATO Black Sea countries remain vulnerable to secessionist conflicts and Russian destabilization, especially through energy dependence. For others such as Turkey, curbing EU enthusiasm endangers reforms and increases the popularity of anti-modern and anti-integrationist Islamist forces.

Pollution and Environmental Degradation

Environmental concerns are another reason for diversifying energy sources and infrastructure. Annually, 145 million tons of petroleum products carried in 9,000 tankers pass through the Bosporus in addition to the enormous traffic in other cargo with expanding trade volumes. The new pipelines bypassing the Bosporus should help to enhance environmental security as well political and economic.

Policy Recommendations: Security

1. Frozen Conflicts. Settling frozen conflicts is a precondition for regional development, security, and NATO integration for the Black Sea region. Disputes must be settled by upholding the territorial integrity of states and the
1. **Frozen Conflicts.** Settling frozen conflicts is a precondition for regional development, security, and NATO integration for the Black Sea region. Disputes must be settled by upholding the territorial integrity of states and the inviolability of borders. Otherwise, precedents could be set that may reverberate throughout the wider region. With the final status of Kosova on the agenda, international players must be alert for pretexts by Russia and its proxies in Moldova and Georgia. Projects should be developed to establish better communication between central governments and secessionist regions. The international community should increase its involvement in border monitoring. The stability of the breakaway entities should be guaranteed by more effective and impartial international peacekeeping forces. Russian troops should withdraw from Moldova and Georgia in accordance with the 1999 OSCE Istanbul commitment.

2. **Regional Cooperation.** Countries in the Black Sea basin are relatively poor, which limits their ability to advance security individually. On the other hand, this is a very heterogeneous territory with multiple players and diverse national priorities. The littoral states, sometimes with conflicting interests, often fail to communicate. There is a lack of trust and credibility, which makes regional cooperation on security issues more difficult. Joint security efforts are necessary, especially in border cooperation, tackling organized crime, counter-terrorism, and dealing with a resurgent Russia.

3. **NATO Membership**
   In general, NATO partnerships and Membership Action Plans have had a positive impact and a stabilizing effect on the region. It is extremely important for regional stability that all Black Sea countries join the Euroatlantic institutions with NATO membership for Georgia, Moldova, Ukraine, Armenia, and Azerbaijan. However, NATO alone would not suffice to solve the region’s security challenges, including the resolution of the outstanding “frozen conflicts” and domestic security concerns.

4. **Wider Security**
   Security issues cannot be narrowed down to maritime security for the littoral states. A broader approach to Black-Caspian security should be considered, including local players such as Armenia and Azerbaijan, and the North Caucasus region, which continues to simmer with conflict and contributes to broader instability.

**PANEL III – EU AND U.S. INVOLVEMENT**

The lack of a comprehensive vision for the Black Sea region is not a shortcoming of the littoral states alone. Euroatlantic players have not developed a strategic plan for the region’s development. It is a main priority for both the U.S. and the EU to act as partners to support democracy, prosperity, and security in a region where both have major security interests.

**European Union**

For the EU, the Black Sea region is a priority by default because after the accession of Bulgaria and Romania, the other littoral states will become the EU’s immediate neighborhood. Chancellor Angela Merkel has indicated that Berlin wants to initiate a comprehensive EU strategy for the Black Sea during Germany’s upcoming EU presidency. The current strategy toward Moldova, Ukraine, and Georgia is designed within the framework of the EU’s European Neighborhood Policy (ENP), which does not envisage further enlargement but deepening institutional and economic cooperation. Although Turkey has been offered EU membership prospects, this is likely to be a long-drawn out process without any guarantees. The EU is also developing a partnership with Russia but faces numerous problems given Moscow’s strategic ambitions in the region.
The EU has several instruments in its approach: it provides various funding mechanisms, such as structural funds and pre-accession funds, and has priorities that it funds and promotes. The Union is involved in local infrastructure and transport projects to enhance roads, railroads, energy, and telecommunications. The EU has backed programs to support economic reforms, civil society, human rights, and the rule of law, and to combat cross-border crime. In addition, various EU projects address security issues and promote European Security and Defense Policy (ESDP) initiatives. The EU supports the liberalization of trade and WTO membership. It is also supporting environment projects to enforce ecological standards. In fulfilling these objectives, the EU works through or together with international organizations such as the Council of Europe (CoE), the Organization for Security and Cooperation in Europe (OSCE), the Black Sea Economic Cooperation pact (BSEC), the South Eastern Cooperation Initiative (SECI), the South East European Defense Ministerial Organization (SEEDM), the Black Sea Forum, the Black Sea Commission, the Black Sea Convention on the Danube, and the Black Sea Task Force on Environmental Protection. The EU does not seek the creation of new institutions to deal with the Black Sea region as there are no shortages of existing ones. At the same time, Brussels is aware of the need to initiate a more active approach. When it comes to enlargement, however, the EU’s immediate ambitions are clearly defined and this has left much of the Black Sea region with an undefined and uncertain status.

The United States

The Black Sea region is also becoming increasingly important for the U.S. The region is a gateway to the Middle East and Central Asia and a key area in the U.S. led war against international terrorists. Until recently, Washington did not view the Black Sea area as a coherent space that needed a specific regional approach. Nevertheless, it has been active in issues such as the “frozen conflicts,” governance, civil society, economic reform, and energy issues. Missing has been a regional vision, with a clear set of objectives and strategies. The U.S. envisages initiatives to enhance democracy building, strengthen the rule of law, promote trade, and enable security cooperation to combat various regional threats. Euroatlantic integration in the Black Sea would clearly underpin American strategic objectives in the region.

When it comes to implementation, not all programs can be rapidly realized. Therefore the U.S. aims to initiate small steps that provide structure, framework, and confidence for addressing larger problems. Moreover, no single regional institution can address the region’s complex challenges. The U.S. wants to support functioning components of existing institutions, rather than the creation of new ones.

Presently, cooperative initiatives in the Black Sea region include the Black Sea Fund, a major project between the German Marshall Fund of the United States and the Romanian government, joint efforts in the U.S. led war against terrorists, the Black Sea Harmony initiative guided by Turkey, the Black Sea Border Security Initiative led by Romania with support from the U.S., and the Black Sea Civil Military Emergency Preparedness Program funded by the U.S. Department of Defense. There are also common efforts to create future global markets for gas through cooperation with Black Sea governments and companies for diversifying energy sources and pipeline ownership.

As to the U.S. military presence in Bulgaria and Romania, Washington has established facilities that allow for American training and forward projection. The U.S. presence will have a positive impact on the military of these two countries in terms of interoperability and modernization. The political implications are also important for the broader region in that the American military presence supports NATO’s mission and provides strategic vision for other littoral countries.
NATO

NATO has a stellar track record in the Black Sea region. Approximately half of the littoral is NATO territory, given the membership of Bulgaria, Romania, and Turkey. Other Black Sea states maintain strategic partnerships and cooperation with NATO. Regarding Ukraine and Georgia, there are no reservations for accession and the doors remain open to any state that can fulfill the requirements for membership. Ukraine’s near term aspirations differ from those of Georgia. Kyiv has domestic political divisions over NATO accession, although NATO is ready to take up the question when Ukraine is ready. Georgia is much more assertive and an intensified dialogue status was granted to Georgia in September 2006 -- an important first step toward NATO entry.

Policy Recommendations: International Involvement in the Black Sea Region

The involvement of international actors such as the EU, the U.S. and NATO in the Black Sea has a positive impact on the region. Despite a number of useful instruments and successful initiatives, Euroatlantic policies have shortcomings that need to be addressed.

The EU’s policies toward the Black Sea have been trifurcated into: enlargement, ENP, and Russia, which undermines its ability to pursue a cohesive regional strategy. The EU also has to combat its own constitutional and budgetary setbacks, which have constrained its ability to act. After the entry of Bulgaria and Romania in 2007, further expansion is likely to be postponed indefinitely. The prospects for EU membership have been the main driving force for reform. Although NATO can help serve as a guarantor of stability and development, Alliance expansion in the Black Sea will also be delayed until the “frozen conflicts” are resolved. This creates gridlock that brings the risk of diminishing reforms, a possible anti-democratic backlash, and increasing vulnerability to Russian pressures.

American strategy toward the Black Sea region must also become more cohesive and wide-ranging. Furthermore, there is some transatlantic disagreement regarding the Black Sea region. While the U.S. pushes for EU integration for most Black Sea countries, the EU complains about its “absorption capacity.” By not working together to effectively resolve the region’s problems the EU and the United States run the risk of underachievement and even policy failure. Missing on both sides of the Atlantic is a comprehensive vision for the Black Sea region with a focus on common transnational issues.

Conclusions

Euroatlantic integration must remain the highest priority for the Black Sea region as the prospect of EU and NATO membership is a major generator for reform in transitional societies. Therefore, keeping Turkey on the EU path and opening the door to NATO for Georgia, Moldova, and Ukraine is essential in order to avoid any reversal in the reform process. At the same time, non-EU and non-NATO members in the Black Sea should continue with implementing reforms in line with ENP and NATO action plans.

The Euroatlantic perspective does not solve all problems of the Black Sea region. The littoral states have a number of local challenges that need to be resolved. “Frozen conflicts” remain a major obstacle for development and their resolution is a precondition for EU and NATO entry with assistance from the international community. The rule of law must be strengthened by reforming the judiciary, improving law enforcement, and applying effective anti-corruption measures. This would encourage economic growth and political stability.
Regarding economic development, privatization, attracting FDI, and modernization of infrastructure should be at the forefront of all government agendas. In addition, restructing the inefficient industries and encouraging entrepreneurship will stimulate growth and decrease the large current account deficits of the states in the Black sea area.

Special attention should be also given to organized crime and trafficking in the region. Energy is another area of special concern both for stability and economic development. The littoral states must make efforts to diversify supplies and sources of energy in order to decrease their dependence on Russia. In tackling these issues, the Black Sea countries should not operate alone but seek ways of cooperating across the region through business links, free trade, environmental protection, and maritime security to combat transborder organized crime, trafficking, and counter-terrorism.

Where possible, Russia should be included in such regional cooperation. There are several common objectives in the security arena in the Black Sea region that also impact on Russia and a dialogue with Moscow could be mutually beneficial. Considering energy issues and the importance of the Russian market, neighboring Black Sea states must learn to anticipate Moscow’s moves and strive to protect their national sovereignty in cooperation with their neighbors and with international institutions. Genuine dialogue cannot be based on economic dependency and political pressure by Moscow.

This publication is based on panelist presentations, supplemented by additional research by CSIS staff. It should be noted, however, that the opinions and recommendations expressed in this report do not necessarily reflect those of the conference panelists. The Center for Strategic and International Studies (CSIS) is a private, non-profit institution focusing on international public policy issues. Its research is nonpartisan and nonproprietary.

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