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Regional Integration in Europe:
Analyzing Intra-Baltic Economic Cooperation
in the Context of European Integration

RAMUNAS VILPISAUSKAS

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**ROBERT SCHUMAN CENTRE
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**Regional Integration in Europe:
Analyzing Intra-Baltic Economic Cooperation
in the Context of European Integration**

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I. INTRODUCTION*

In the beginning of the 1990s, Estonia, Latvia and Lithuania re-emerged as independent actors in the international system. Policy makers of these three Baltic countries were faced with a range of options in choosing their cooperation partners and forms of cooperative arrangements best suited for their particular needs and interests. The decisions had to be taken in the environment of changes in international security and the economic order as well as domestic economic and political reforms accompanied by the establishment of new rules and institutions.

The choice of foreign policy priorities was to a large extent determined by the aims of political and economic reforms (transition to the market economy and democratic governance) and perceived external threats and opportunities. Thus, membership in the European Union (as well as other international and regional organizations and regimes) soon emerged on the top of the agendas of the leaders of the three Baltic countries. Intra-Baltic relations have been relatively important even before the re-establishment of independence and to a varying degree remained so until now¹. Intra-Baltic relations have been formalized in a number of trilateral agreements, while signing bilateral agreements with the EU, implementation of pre-accession arrangements and the beginning of accession negotiations with one of the Baltic States paralleled this process and extended integration further in scope and depth.

However, factors accounting for the *choice* of general cooperative policy orientation do not necessarily provide an explanation of *dynamics* of cooperation and the particular forms it assumes. This paper addresses policy developments that in general terms can be defined as the impact of a large regional arrangement on small neighboring countries and their cooperative dynamics, and interaction of regional integration and sub-regional cooperation processes. In more concrete terms – to what extent can the EU's policy account for the development of intra-Baltic economic cooperation? Does the role of the EU explain the timing and the forms of the Baltic economic agreements, the

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¹ Intra-Baltic, or sub-regional cooperation in this paper refers to cooperation among Estonia, Latvia, and Lithuania.

successful conclusion of some cooperation schemes, for example, free trade and the removal of non-tariff barriers, and the failure of others, namely, a customs union? Or does a satisfactory explanation of the cooperative dynamics among the Baltic States and instances of protectionism, or non-cooperation, need to include other factors, for example, sub-national interest groups or transnational actors? How do the characteristics of transition of the three countries influence the dynamics of regional cooperation? Finally, how is further integration into the EU likely to affect cooperation among the Baltic countries?

These are the main issues that are discussed in this paper. Baltic cooperation provides an interesting case study for testing the propositions of regional integration and cooperation theories, political economy approaches and explanations of transition dynamics. However, first an overview of the literature on Baltic cooperation will be presented to provide a picture of the “state of art”, and to expose the gaps that this study aims to fill. It will be followed by the presentation of a framework of analysis to be used in this study, and the empirical part, which will test the propositions by analyzing dynamics of intra-Baltic economic cooperation since the beginning of the 1990s. The paper will conclude with the outline of possible future cooperation dynamics among the Baltic States.

II. EXPLAINING INTRA-BALTIC COOPERATION

The intra-Baltic cooperation has been increasingly attracting the attention of both local and foreign analysts, which have resulted in a number of papers dedicated to this issue. Most writings on intra-Baltic cooperation have focused on the military and security issues or geopolitics of the Baltic region². The level of intra-Baltic cooperation is seen as a function of external threat and the balance of powers in the European or Trans-Atlantic “security architecture”, the geographical position of the three countries, historical experiences and links, size of the Baltic States, or internal resources. Usually a combination of the above-mentioned factors is analyzed, and most of the analysis exhibits methodological features of the realist tradition in analyzing international relations³.

² See, for example, Ozolina (1994), Van Ham (1995), Bleiere (1997), Lejins (1997), Stranga (1997), Rebas (1997/1998), Van Ham (1998), Kreslins (1998), Laurinavicius and Motieka (1998), Made (1998), Ozolina (1998). The majority of references provided in this paper are writings published in English with some sources (mainly periodicals) in Lithuanian.

³ One particularity common to the majority of writings on inter-Baltic relations is explicit or implicit emphasis on “regional identity” or “regional awareness” of the Baltic countries resulting from cultural, historical or linguistic characteristics. While this constructivist tendency is displayed by many scholars, it is often mixed with rationalist arguments and recommendations. Another frequent feature is a normative tone implying desirability of cooperation. This paper presents a positive political economy analysis.

A number of writings have analyzed institutional aspects of Baltic cooperation, thereby diverging from the realist image of international relations⁴. A level of institutionalization of Baltic relations is perceived to be a function of institutional capacity and functional scope, or convergence of national interests. The role of sub-regional Baltic institutions is usually compared to the national decision-making institutions, and by implicitly considering regional institutions as factors influencing and fostering cooperation, these writings supplement those centered around the unitary state actors and balance of power in interstate system.

Finally, some analysts have discussed the dynamics of intra-Baltic economic relations⁵. This type of analysis draws on theories of regional economic integration or concepts of international trade and factor movements in general. The unifying assumption is a causal relationship between regional economic arrangements and the economic welfare of the countries. The interest in intra-Baltic trade agreements has been related to the importance attached to international economic relations for economic reforms and growth of small and increasingly open Baltic economies. Calculations of, for example, trade creation (or diversion), though, have not been produced due to a number of reasons, including the transitional character of Baltic economies and the quality of statistical data.

This brief overview of the literature allows several observations. First, analysts attribute major importance to security factors in explaining cooperation among the Baltic countries, and especially their efforts to integrate into the EU. Their importance in explaining Baltic countries' foreign policies is not disputed here. However, while security considerations might provide a strong impetus for choosing certain cooperative options and goals, it explains only the initial decisions to cooperate but can not explain the development of cooperation, and particular forms it takes. Certainly, there are possibilities for external forces to change the perception of the security situation and to alter the cooperative dynamics. For example, a major negative reaction of Russia towards the invitation of a Baltic country to join NATO might push the Baltic States' cooperation towards a deeper level (not only in the military cooperation field but also in the economic area) or towards reinforced integration efforts into the EU. To provide a recent example, events in Russia in September 1991 and the attempted *coup d'état* have been interpreted by some as a major factor behind the EU recognition of the Baltic States. However, radical changes in the external security environment can not explain the starts and stops of intra-Baltic economic cooperation. Moreover, systemic explanations focused on security

⁴ See, for example, Jurkynas (1998), Kapustans (1998).

⁵ See Lesser, Muravskaya and Shumilo (1997), OECD (1996), Pautola (1996), Sorsa (1997), Vilpišauskas (1998).

factors usually downplay the importance of domestic factors. Therefore, the importance of security motives is recognized but this factor is taken as given during the period analyzed.

Second, the emphasis on historical legacies or norms and identities has similar drawbacks. They might explain certain tendencies, commonalities or differences in actors' behavior but they do not seem to be able to account for incremental policy developments. For example, the argument of "European identity" might to a certain extent explain "back to Europe" policies of Baltic policy makers. Also, the argument of the "lack of common Baltic identity" could be used to account for divergent perceptions and foreign policies of the three states. However, such factors can not plausibly explain why the free trade area and not a customs union has been established among the Baltic States. Historical legacies and culture can rather be treated as constraints within which actors take decisions. It is not implied that explanations of policy developments in the Baltic countries based on cultural or historical factors (as well as security or geographical factors) are wrong. They are just irrelevant for explaining the dynamics of economic cooperation among the Baltic countries (as well as the dynamics of their integration into the EU).

Third, theories of economic cooperation and integration can explain and predict the possible impact of economic agreements on the welfare of countries involved or third parties. Thus, they can provide an understanding of policy makers motivations for using economic agreements for achieving their political aims. They can also explain the possible impact of the integration of markets or lack of it on domestic and other actors. However, they do not (seek to) provide "explanations of the political choices that produce integrated areas"⁶. Their insights need to be incorporated into the wider framework that allows analysis of the development of the cooperation/integration processes, and the role of actors and institutions involved. This is discussed in the following section.

III. FRAMEWORK FOR ANALYSIS

A. Conceptualizing Cooperation

The issue of why nations cooperate and integrate has been discussed extensively by international relations scholars⁷. As it was illustrated above, a number of

⁶ Mattli (1999:19).

⁷ Interestingly, this issue used to be approached in the reverse form in the Baltic States – "why don't we cooperate?" While this tendency could be explained by the coordinated position in regard to relations with Russia during the years of independence movements, the present state of affairs renders such phrasing of the question increasingly irrelevant. However, it does mean

perspectives have been applied to explain intra-Baltic cooperation. This paper offers a different perspective and analyses intra-Baltic economic cooperation by employing concepts drawn from liberal explanations of international cooperation and the political economy of regional integration. This section proceeds by first defining the dependent variable of economic cooperation of the Baltic States. Afterwards the independent variables are discussed. The focus is placed on the effects of the EU policies, which, it is argued, have been a major factor behind intra-Baltic economic cooperation. However, to explain the dynamics of intra-Baltic economic cooperation, in recent years in particular, domestic factors have to be taken into account. Progress in transition during which the formation of new groups advances and institutional channels for voicing their preferences are being formed seems to allow increasingly for an articulation of market demands both for and against integration of national economies. To use the metaphor of games theory, games are played on international level among Baltic governments and Baltic governments and the EU, and domestically⁸. Finally, the definition of actors and processes is followed by a number of propositions regarding the dynamics of the intra-Baltic cooperation.

This paper adopts the definition of international cooperation suggested by Keohane, which has gained wide acceptance among scholars of international politics. Keohane maintains that cooperation "takes place when the policies actually followed by one government are regarded by its partners as facilitating realization of their own objectives, as the result of a process of policy coordination"⁹. As Milner observes this definition assumes "that an actors' behavior is directed toward some goal(s)"¹⁰. Therefore, analysis of cooperation requires understanding of how particular objectives are formed and prioritized. Regional cooperation might facilitate achieving of goals that have their targets both in the external environment and domestic arena. Second, it implies "that actors receive gains or rewards from cooperation"¹¹. Thus, the issue is how the distribution of gains is perceived by participating actors, and how cooperative measures influence chances of achieving other objectives of governmental actors as well as the distribution of gains among domestic economic groups.

that Baltic cooperation has not originated from 'the state of non-cooperation' but has its origins in recent coordination practices. This experience is likely to act as a facilitating factor.

⁸ The assumption is that domestic politics matters even when actors respond to external effects, and that both international and domestic levels of analysis can be combined into coherent analysis. See Evans, Jacobson, Putnam (1993).

⁹ Keohane (1984:51-52).

¹⁰ Milner (1997:7).

¹¹ Ibid.

Intergovernmental cooperation varies in issue scope and form. However, economic cooperation in one particular area, for example trade matters, is likely to have political effects and facilitate achievement of other political objectives. As Feldstein has stated, "economic cooperation is part of the more important process of international cooperation"¹². This is certainly true in the Baltic case. Economic cooperation acquires political meaning, and may also serve to achieve political objectives. Sub-regional economic cooperation is seen and supported by the EU as an important condition or supplement to the stability and security of the region. Therefore, although this paper focuses on intra-Baltic economic cooperation, its political significance, as it will be argued later, derives from the importance attached to it by Baltic States' leaders as a means of advancing other objective - integration into the EU. Especially, since "most of the economic arguments favoring regional integration are not met by integration among the Baltic countries"¹³. Thus, the level of economic interdependence does not seem to have provided a strong case for policy coordination and market integration.

Furthermore, analysis is focused on cooperation in the area of economic exchange. The choice is based on several grounds: (1) it has probably been probably the most advanced area of intra-Baltic cooperation, in some aspects surpassing multilaterally accepted requirements for regional agreements¹⁴; (2) it is characterized by both successes and failures allowing different outcomes of cooperation dynamics to be compared; and (3) it illustrates how the domestic politics matters even when cooperation objectives are strongly motivated by the external environment. *The dependent variable is the scope of intra-Baltic cooperation in the field of economic exchange, or market integration*¹⁵. It comprises both agreements to cooperate and failures to cooperate which include unilateral, competitive or conflicting behavior lowering benefits to other actors as well as inactivity¹⁶.

¹² Feldstein (1988:9).

¹³ Sorsa (1997:16).

¹⁴ The main requirements for regional agreements set by the GATT include reduction of trade between the constituent territories within a reasonable period of time and no increase of barriers to third countries. Trilateral agreements signed among the Baltic states have not foreseen any transitional periods, eventually trade liberalization was extended to trade in agricultural goods which is usually exempted from similar agreements.

¹⁵ There is a widely accepted differentiation between "negative" or "shallow" integration and "positive" or "deep" integration. The former refers to removal of tariff barriers to exchanges at the border, while the latter refers to harmonization of rules and conduct of common policies, or removal of behind the border barriers. (see Kahler (1995), Pinder (1968), Wallace (1994).

¹⁶ Milner (1997:8). In the case of the Baltic States, the issue has often been framed in terms of cooperation versus competition, leading some to conclude that "we are economic competitors" (Made 1998:38). In many cases, Baltic policy-makers as well as analysts tend to extend the model of competing firms to the level of the three countries, mix the notions of

Cooperation can be pursued in different forms and in different settings. It may vary from *ad hoc* measures to agreements having long-term effects, to creation of common institutions that further facilitate cooperation by reducing transaction costs and uncertainty, limiting asymmetries of information, or even acquiring an independent role in the policy-making process. In the Baltic case, several institutionalized settings – the Baltic Council of Ministers, the Baltic Assembly, and the Baltic Council – provide opportunities for regular policy coordination and negotiating of trilateral agreements. The fact that these regional institutions do not possess independent authority differentiates the Baltic cooperation from the Baltic countries' integration into the EU, with the latter implying not only linking of economic domains and participation in common policies, but also eventually delegating authority to the supranational institutions¹⁷.

B. The Impact of a Regional Union on Neighboring Countries

The observation that the EU has been having an important effect on intra-Baltic cooperation is not new¹⁸. Surprisingly, a systematic analysis of this causal effect as well as possible future developments has been absent. In other words, what is the impact of the EU on the cooperative dynamics of neighboring countries? And what insights can integration studies offer for this type of analysis?

Regional integration, and the EC/EU in particular, has been analyzed extensively by scholars of political science and economics. However, the issue of the external effects of integration is “a topic that both political scientists and economists have mostly overlooked”¹⁹. As a rule, analysis has been limited to a fixed number of participants and their integration choices without extending theorizing to include its impact on external actors, and their responses. This applies to both “classical” perspectives on integration advanced by political scientists – neo-functionalism and intergovernmentalism²⁰. “New” political approaches to regional integration – liberal intergovernmentalism, multi-level governance or reformulated versions of neo-functionalism – have been mainly focusing on explaining advances of integration in scope and level inside the

firms' competition with states' competition for status and prestige, and locational competition for FDI - issues which could be an interesting matter of a separate analysis.

¹⁷ The differentiation between the terms “cooperation” and “integration” in this paper refers mainly to the level of institutionalization, thereby distinguishing between trilateral Baltic states relations and their individual policies towards the EU aimed at eventual membership.

¹⁸ For example, Lainela and Sutela (1994:11) have suggested, that “the Baltic free trade agreement of September 1993 is largely due to outside European pressures”.

¹⁹ Mattli (1999:59).

²⁰ Although in his reformulation of “pretheory” of regional integration Haas (1971) has discussed the possible impact of “external world” on the dynamics of regional groupings, this factor was not conceptualized.

EC²¹. Although successive enlargements of the EC/EU have received considerable attention, the main issue has been, to use Gower's expression, "the old academic chestnut" on the interrelationship of widening and deepening²². Thus, the emphasis has been on the impact of the enlargement on the status and prospects for further integration inside the EC/EU.

Differently, economic perspectives on integration have addressed its impact on external actors, mainly by employing the concepts of trade creation and trade diversion²³. In addition to traditional welfare-oriented explanations, recently other forms of "nontraditional" gains from regional trade agreements, for example, bargaining power, which link regional integration to external environment have been discussed²⁴. These recent explanations represent a part of a broader interest in regional integration and regionalism that has increased after the acceleration of integration in the EC in 1980s and a wave of new regional agreements in 1990s. While suggestions of economic theories of integration regarding possible effects of market integration are employed to explain the likely impact of this process on domestic economic groups, some arguments, for example the bargaining power argument, do not seem to apply to the Baltic case.

A recent example of an inclusive approach explicitly addressing the external effects of integration is a general explanation of regional integration suggested by Mattli²⁵. This paper adopts some of his observations, although with significant modifications. Therefore the argument is briefly presented first, followed by suggested modifications that seem to be appropriate for the Baltic case²⁶. Mattli argues that for an integration scheme to succeed, two sets of conditions need to be satisfied – demand side and supply side conditions. The demand for regional rules, regulations and policies by market players seeking to

²¹ Though there are exceptions. For example, Friis and Murphy (1997) address the external role of the EU using the multi-level governance approach. One of recent examples of applying "classical" political integration perspectives to EU enlargement is in Balazs (1998).

²² Gower (1999:8).

²³ See Viner (1950). The concepts of trade diversion and trade creation have remained popular and are used to estimate the possible welfare effects of economic integration. For a general theory of economic integration see Balassa (1961).

²⁴ See, for example, Fernandez and Portes (1998), and Ethier (1998) on the new regionalism. For an analysis of recent regional trade agreements centered around the EU and "me-too" effects, see Pelkmans and Brenton (1997). The external impact of regional economic integration has been addressed by Baldwin (1995) in the framework of "domino effect" applied to the study of EFTA countries' response to deepening of integration in the EU. Later Baldwin (1997) has extended his "domino" explanation of regionalism to the other regional schemes.

²⁵ See Mattli (1999). For other recent political economy approaches to studies of regional integration and regionalism see Mansfield and Milner (1997).

²⁶ The presentation is based on Mattli (1999:41-67).

internalize externalities that arise from economic and political uncertainty is the driving force of regional integration. Furthermore, the potential gains from market exchange within a region must be significant. The second condition for integration to succeed is the willingness and ability of political leaders to accommodate demands for deeper integration. Willingness depends on the economic situation and growth prospects of the home market. Ability in turn depends on solving collective action problems, which is facilitated by an existence of "commitment institutions" and a regional leader – a dominant member state of a regional grouping – acting as a focal point of coordination and "paymaster" easing the distributional tensions. The presence of these conditions is likely to make integration efforts successful. A successful regional integration is likely to have an impact on outside countries by creating externalities such as the loss of market access and investment diversion. Outsiders, especially during economic slowdowns, seek to join the union – "the first integrative response". However, if the union has no incentive to accept new members, they might respond by creating their own regional group – "the second integrative response". For this project to succeed again demand and supply conditions need to be met.

This paper builds on the basic premises of the approach suggested by Mattli. It considers the conditions of governments' willingness and ability to cooperate as well as the market demands. Particular importance is attributed to the role of leadership and the "commitment institution" in solving coordination problems by providing common rules and side-payments. However, the arguments are modified and supplemented in several respects. It is argued that the role of the leader can be played by the external regional union, which the neighboring countries aspire to join when a clear leader is lacking among the sub-regional states. The external group – the EU in this case – provides rules for intra-Baltic cooperation thereby facilitating the choice between multiple equilibria over which members of sub-region might have diverging interests. The leadership role of the EU is backed by financial assistance. However, in both respects the role of external leader is limited. The provision and adoption of the rules for sub-regional cooperation depends on the prospects of integration of individual countries into the regional union. Thus, willingness to cooperate depends not so much (or not only) on economic gains but on the facilitation of integration into the regional union. While the financial assistance can facilitate the administrative aspect of sub-regional cooperation, it is not sufficient for side-payments for the domestic groups dissatisfied by redistribution. Furthermore, the analysis is extended to include demands against integration, not only for it as well as transition related issues such as uncertainty, lack of resources and changes in political and economic institutions which impacted on both the ability of governments to cooperate and the channeling of market demands. Finally, "the second integrative response" is seen as a complimentary rather than

an alternative policy of sub-regional cooperation. The dynamics of sub-regional cooperation is directly conditioned by the prospects and prerequisites for integration into the regional union. The assumptions and propositions are presented in detail below. The starting point of the analysis is a modified "second integrative response".

To present a simplified picture, the outside countries for a number of reasons express their willingness to join the regional integration scheme. For a number of reasons, the regional union finds it too costly to accept new members but does not deny the possibility of doing so some time in the future. Meanwhile it encourages outsiders to cooperate amongst themselves and supplies the schemes of market integration as well as financial support and leadership. Thereby it acts as a push factor for outsiders' cooperation, which is also facilitated by certain conditions (the security situation, recent cooperative experiences, and common objectives, the demands of actors' benefiting from integration), and is disturbed by other factors (divergent preferences to achieving policy objectives, protectionist demands of actors standing to lose from market integration, etc.). This paper addresses the impact of (1) regional union which outsiders aspire to join and of (2) domestic actors' preferences on sub-regional cooperation. The other factors are taken as given.

The impact of a regional union on the scope of sub-regional cooperation of neighboring countries can be assessed by examining the union's policy towards individual countries and how particular decisions addressed to them as a group or individually affect sub-regional cooperation. The analysis would be incomplete, however, without examining the responses of the sub-regional group and how they translate into further supply of sub-regional cooperation or the lack of it.

This analysis establishes a clear link between sub-regional cooperation and the policies of the regional union. As it was indicated above, sub-regional cooperation is perceived by participating actors not as an alternative but as a facilitator of individual integration into the regional union. For the purposes of this analysis, integration refers to the process of an independent state joining the regional union by way of removing barriers to free exchange and movement of factors of production (negative integration), adoption of certain common rules and policies (positive integration), delegation of authority to supranational institutions and participation in the common decision-making procedures. Thus, unilateral adaptation rather than joint decision-making is emphasized. The focus of analysis is on sub-regional actors, and their strategies vis-à-vis the neighboring regional union. Integration refers to a gradual process evolving in stages that can be identified for analytical purposes. The integration process includes: (1) the establishment and intensification of diplomatic and economic

relations, (2) a pre-accession stage when the union explicitly acknowledges the possibility of eventual membership, and supplies schemes designed to prepare applicants for integration into the common market and accession, (3) the accession negotiations during which individual applicants agree with the union on the (negotiable) conditions of membership, and further proceed with adoption of rules governing the common market and common policies, (4) the accession itself after which the new members acquire the right to participate in the decision-making procedures but may have transition periods in certain areas. The main proposition is that there is a link between integration of individual members of the sub-region into the union, and the dynamics of sub-regional cooperation. Participation in the different stages of integration implying divergent prospects of union membership is likely to act as a barrier to cooperation and encourage non-cooperative policies.

C. Cooperation Policies and Institutional Transition

The basic assumption of the analysis is that governments act as utility maximizers, and are willing to cooperate when (regional) cooperation is likely to promote the chances of achieving their objectives²⁷. For cooperation to occur governments should be both willing and able to cooperate²⁸. While willingness depends on how cooperation measures are perceived to influence achieving other objectives, other policy goals more specifically, or reelection chances more generally, their ability to cooperate depends on resources available and a leader that could serve as a focal point of coordination of rules and policies. However, governments, as well as other actors, act in concrete institutional and organizational settings and power configurations, both domestic and international, which structure their behavior. They can be constrained by resources available to them, including finances and expertise. Both of these factors have set particularly important limits on actors' behavior during the transition process. The role of governments has been highly complicated during the transition period characterized by high uncertainty, information

²⁷ This assumption of rational actors can be criticized in general, and specifically as applied to the transition countries. For a reflectivist ("sociological institutionalist") critique of rationalist premises applied to the EU enlargement see Schimmelfenning (1998). More specific disagreements as applied to the analysis of transition economies can be distinguished. For example, policy makers characterized as "technopols" might be motivated by concerns for "general good" and think that "there are more important things in life than remaining in office" thereby disregarding the re-election consequences of their policy that are assumed to be the main concern of policy-makers in times of "normal" politics (Williams 1994:22). Certain other constraints on actors' behavior are discussed in the text. Still, "by starting with the assumption of ... rational motivation we may obtain predictions that serve as a useful benchmark by which to assess the extent and impact of other actions" (Hardin cited in Mattli 1999:16-17).

²⁸ Mattli (1999:42)

asymmetries, a lack of expertise and other resources, or in more general terms, instability resulting from a radical change of political and economic institutions²⁹.

Faced with uncertainty and lacking resources, Baltic governments have been more likely to follow external advice and adopt existing regimes governing economic relations. Moreover, unilateral, or to use Nicolaidis' term, "anticipatory adaptation" of regimes governing economic relations of industrialized democratic countries was at the basis of transition to market economy and democratic governance³⁰. It formed a part of the learning and imitation process of the policy makers in transition countries and expressed itself in, for example, advocating the direct import of other cooperation models or protection patterns³¹. This process of adaptation to a large extent has been taking place irrespective of external demands³². However, the external coordinator has proved to be necessary in order to overcome problems of coordination, and to agree on specific forms of sub-regional cooperation.

The EU by virtue of the importance attached to it by Baltic leaders has been playing a role of external coordinator in this process by providing rules for regional cooperation and domestic policy-making, often in close coordination with other suppliers of aid, trade or financial regimes. The role of the EU as an external coordinator helped to solve coordination problems of intra-Baltic cooperation when the three were all "vaguely and diffusely in favor [of cooperation], but their preference for forms and terms make agreement on the specific cooperative enterprises difficult"³³. Coordination problems have particularly hampered intra-Baltic economic cooperation during the first years of the decade. The prospect of EU membership, integration based on the rules supplied by the EU and the realization that sub-regional cooperation is likely to advance integration into the EU, have all played a role in designing and implementing schemes for intra-Baltic economic cooperation.

²⁹ As one transition expert has maintained, "[T]he essence of both political and economic transition is a change in a country's institutional system" (Balcerowicz 1997:153).

³⁰ Nicolaidis (1993).

³¹ Nordic regional cooperation institutions or the Benelux model have been often referred to as the ones to be followed by the Baltic States.

³² And has often resulted in a mixture of "positive reference models" (Offe 1996:212-213) both from the external environment and from the past. For example, inter-war cooperative experiences have often been referred to in the discussion on the models of intra-Baltic cooperation.

³³ Jurgaitiene and Waever (1996:215).

D. Motivations

The motivations of the Baltic States of the joining the EU present a mixture of ideological, historical, security and economic reasons. The officials of the three states have repeatedly stated the importance of "promotion of the economy, growth and development", "security aspects", "social welfare", and "participation in common European matters"³⁴. Although the importance of security, identity, history and international status is not disputed, and they have been acting as a major initial force for the orientation of the Baltic states' foreign policies towards the EU, the emphasis in this paper is on economic factors. The EU has been perceived as a center of economic prosperity and as a source of economic modernization for the Baltic economies. Its importance as a source of economic opportunities and resources (finance, market access, expertise, and rules) has provided a strong impetus for prioritizing the membership in the EU as the highest priority of Baltic States foreign policies. At the same time, given its more limited opportunities intra-Baltic economic cooperation has come to be seen as instrumental for advancing individual countries' integration into the EU³⁵. Intra-Baltic cooperation for a number of reasons including history, identity, security, etc. has been on the agenda since the re-establishment of independence and entry of the Baltic States into the international system. Advances in the field of sub-regional economic cooperation have, however, been directly linked to EU policy towards Central and Eastern Europe, and the Baltic sub-region in particular, and to the utility attached by the Baltic states' governments to the sub-regional cooperation as maximizing their chances of integration into the EU³⁶.

The EU's policy towards the Baltic States has also been based on a mixture of motives and factors. As has been the case in EU policy towards Central and Eastern Europe in general, it has resulted from a complex interaction of EU institutions, member states, interest groups and external actors all motivated by their own security, economic and other interests and considerations. This process has received considerable attention, and it is

³⁴ From the presentations of officials from the respective Ministries of Foreign Affairs in the conference "The Baltic Dimension of European Integration" in Riga, August 24-25, 1996.

³⁵ The same argument could equally, or even more strongly, be applied in case of security motivations. EU membership is perceived by the Baltic States to give better chances for providing the public good of security than intra-Baltic cooperation.

³⁶ In this respect, strong parallels can be found in the case Visegrad countries and creation of the CEFTA in particular. However, there seem to be important differences among the Baltic States and CEFTA countries in both the level of institutionalization of sub-regional cooperation and the scope of sub-regional market integration. The comparative analysis of these two sub-regions and their dynamics could be an interesting issue in itself.

beyond the scope of this paper to address this issue³⁷. What is important for this analysis is not the factors behind the development of the EU's policy towards the Baltic States but its content and forms towards the Baltic States as a sub-region and individually *which have impacted on the intra-Baltic cooperation*³⁸. Thereby the paper emphasizes the importance of the EU as a regional actor represented by its institutions, particularly the Commission "who played the pivotal role as the guardian of the process of rapprochement of Western and Eastern Europe", and in forming of EU's policy towards the Baltic States³⁹. The picture risks being incomplete without taking in account the policies of certain member states that have showed a strong interest in the matters of the Baltic countries, in particular the Nordic countries and Germany. Most of them are geographically close to the Baltic States and have particularly strong security and economic interests in intensified intra-Baltic cooperation. However, their interests have translated into the policies towards the Baltic States mainly through the bargaining processes inside the EU. As was noted, this paper leaves out the question of how EU policy towards the Baltic States has been formed and developed, and what actors and interests have shaped it.

E. Market Demands

The EU factor alone, it is argued, does not account for the starts and stops of intra-Baltic economic cooperation. Recent developments have shown that economic interest groups have an increasing influence on intra-Baltic cooperative policies, and their influence is likely to increase in the future. Market integration measures have a direct impact on economic actors' activities, with some standing to gain from the removal of barriers to exchange and the reduction of transaction costs and with others standing to lose because of likely redistribution effects. This creates incentives for economic interest groups to lobby for or against further integration. The role of economic interest groups in advancing integration in the EC/EU has been widely acknowledged⁴⁰.

³⁷ For critical analysis of EU's policy towards Central and Eastern Europe see Kramer (1993), Sedelmeier and Wallace (1996), Zielonka (1998), Gower (1999); for insiders' views see Avery and Cameron (1998), Mayhew (1998).

³⁸ Motives for the EU to promote sub-regional cooperation among applicant countries have been summarized by Inotai (1997:14-15), and include expectations that sub-regional cooperation would serve as a training ground and learning process for EU membership, geopolitical and security interests and interests in easier market access for its goods and capital.

³⁹ Amswald (1998:22).

⁴⁰ The pro-integrationist role of economic interest groups have been given central role in the neo-functional account of the early EC integration. For recent explanations of EC/EU integration dynamics emphasizing the role of economic interest groups see Mattli (1999), Sandholtz and Zysman (1989), Sandholtz and Stone Sweet (1998). Of course, the main

Importantly, as it was noted several decades ago “the list of ... actors should include not only groups which perceive themselves benefited by integration but also groups opposed to it...”⁴¹. It is often assumed that economic groups characterized by higher degree of internationalization – export oriented, participating in intra-industry trade, multinational enterprises – are more likely to support market integration measures or “resist protectionism”⁴². Enterprises using local resources and selling their products in the domestic market are more likely to call for protectionist measures under the actual or anticipated pressure of adjustment. Thus, various domestic groups are likely to “demand different policies, and a government’s economic policy choices often will reflect the underlying preferences of the strongest and best-organized interests within society”⁴³.

The relative absence of the activities of economic interest groups in the context of intra-Baltic cooperation, in particular those favoring integration, and a resulting lack of their analysis, can probably largely be explained by the transition process itself and the initial non-existence of functioning markets and institutional channels of voicing their demands. At the outset of the political and economic reforms, changing rules and institutional structures have, although to a different degree in different states, deprived economic groups of their former influence. As some have noted about the transition process in Central and Eastern Europe, “the new economic and political environment confronted all interest groups with a loss of power”⁴⁴. Moreover, in the Baltic States popular perception has largely identified the support for transition goals with the support for the re-establishment of statehood which has reinforced opportunities for “extraordinary politics”, and provided policy makers with more room for policies disadvantaging special interests⁴⁵.

difference in the Baltic case is the absence of a supra-national institution towards which transnational groups direct their demands.

⁴¹ Nye (1971:197).

⁴² Milner (1988). It should be noted, however, that foreign investors in certain cases are likely to demand protection, as has been observed in some CEECs. See Winters (1995).

⁴³ Mansfield and Milner (1997:12).

⁴⁴ Bofinger (1995:21). This observation seems to be in line with Olson’s argument that radical changes in societies destroy rent-seeking organizations for collective action. Interestingly, applying his theory to the transition countries Olson himself has used his argument in a different manner stating that “since the enterprises and industries are not destroyed by the transition to democracy, but are, on the contrary, given a new freedom to lobby for their sectional interest, this problem is magnified during the transition” (1996:77). The issue seems to be whether the conjuncture was critical enough to completely destroy channels of influence established during the previous regimes.

⁴⁵ Norgaard (1996).

These opportunities, resulting from a conjuncture of the above mentioned factors, were exploited to a different degree in the three countries depending on the structures of national economies, institutional structure of policy-making, ideological commitments and reform strategies. For example, relatively large agricultural sectors in Lithuania and Latvia have allowed agricultural interests to exert larger influence on policy-makers. The greater amount of large-scale, outdated industries in these two countries also seemed to generate stronger protectionist interests, which have been indicated as an important constraint to the adoption and implementation of economic policies⁴⁶. In contrast to Estonia and Latvia, in Lithuania possibilities to introduce legal changes to the trade regime by decree has made it easier for interest groups to influence government's policy. Governments headed by economic technocrats have been less vulnerable to economic interest groups while governments formed as a result of "protest vote" have been more reserved towards market integration and more inclined to support large disadvantaged groups (votes) and better organized lobbies (funds).

The latter phenomena could be observed in particular after a certain stability of newly established political institutions has been achieved. New institutions "gradually produce their own social and economic basis"⁴⁷. Policy-makers learn how to take advantage of possible promises of votes or funds. Disadvantaged or newly created groups learn how to play to the new rules of the game to advance their interests by using newly established interest-intermediation structures, preserved old connections or voicing open protests. Although the protests often had their source in the general economic situation, resulting from a decline in production and incomes levels, they have frequently expressed themselves by targeting the liberalization of international economic transactions and specific policies of intra-Baltic market integration. The patterns of lobbying have to a large degree been dependent on the speed and openness of privatization which created opportunities for (or prevented from) influencing policy-making and implementation and receiving special privileges.

The other explanation for a relative absence of observed market demands for intra-Baltic market integration lies in the small size of the sub-regional market. The three states combined form a market of around 8 million consumers. At the start of reforms, intra-Baltic trade has made up only several percents of the total foreign trade share in each of the countries. Although the volume of intra-Baltic trade has been increasing, its share has remained comparatively small despite trilateral free trade agreements signed. Therefore, the relatively small potential for economic gains from market exchange might

⁴⁶ Norgaard (1996:162).

⁴⁷ Norgaard (1996:3).

have reduced incentives for lobbying for further integration⁴⁸. Since such labor-, skill- and resource-intensive industries as clothing, footwear or textiles favor small and flexible units of production, possibilities for economies of scale in the region seem be limited at present⁴⁹. Recent developments in foreign direct investment in the Baltic States and intra-Baltic investments might signal new tendencies of informal integration. Increasing involvement of foreign investors who treat the Baltic States as one market, internationalization of Baltic companies and signs of market concentration, for example, in the financial services sector, might exert indirect pressure on governments to proceed with removing non-tariff barriers and harmonizing market regulations by using EU rules as a basis. Except occasional statements, so far visible lobbying by these groups for further market integration has been absent.

Much more visible have been demands for protection which recently have led to an exchange of protectionist measures among the Baltic States assuming a pattern of tit for tat policy⁵⁰. These (non-tariff) protectionist measures were taken in response to the lobbying by local economic interest groups that experienced adjustment problems as a result of economic crisis in Russian markets. Crisis "may bring new players into the game", or provide an opportunity for previously ignored groups to advance their own interests⁵¹. Because of their size, the Baltic States rely heavily on international economic exchanges, and in respect to Russia and the EU all three states are characterized by very small influence capability and high degree of sensitivity⁵². The economic crisis, which started in Russia in the summer of 1998, have caused a decrease in sales of Baltic exporters, and triggered their demands for protectionism. To rephrase Winters, adjustment pressure caused by the fall of demand in one market can translate into a greater pressure for protection from another⁵³. The issue has become linked to intra-Baltic economic cooperation and is managed by manipulation of non-tariff barriers, namely product standards and administrative rules, to satisfy the demands of local producers, mainly agricultural groups. These developments have cast a new light on the political economy developments of intra-Baltic economic cooperation and have shown the limits of the EU acting as an indirect coordinator and leader.

⁴⁸ Mattli (1999:42). This argument also works for the supply side – governments might be less willing to advance market integration if it does not promise to improve significantly economic welfare. Intra-Baltic market integration developments illustrate, however, that it is not a necessary condition and other factors might be at work.

⁴⁹ Pautola (1996:15).

⁵⁰ In game theory terms, tit for tat is the policy of cooperating first and then doing whatever the other player did on the previous move (see Axelrod 1984).

⁵¹ Nello (1997:17).

⁵² On discussion of these concepts see Peterson (1998).

⁵³ Winters (1995:2).

F. Propositions

To sum up the main arguments and sketch the directions for the empirical part this of analysis the following propositions are presented:

1. The scope of intra-Baltic economic cooperation has been determined by the EU and by the demands of domestic economic interests groups. Each factor can facilitate or obstruct sub-regional cooperation depending on the conditions specified.

1.1.1. The EU has acted as the supplier of sub-regional cooperation rules and as the indirect "supervisor" of sub-regional cooperation. The EU has also supplied financial assistance, although restricted to administrative aspects and pre-accession measures.

1.1.2. The EU initial strategy of parallel and uniform treatment of the Baltic States and its emphasis on sub-regional cooperation as an informal precondition for membership has gradually changed with the evolution of enlargement politics and emphasis on the individual achievements of applicant countries. The group approach towards the Baltic States facilitated intra-Baltic economic cooperation, while the differentiation proved to discourage it.

1.1.3. The issue of intra-Baltic economic cooperation has been high on the agenda of Baltic leaders since before and after the re-establishment of independence. However, after the establishment of relations with the EU it has become instrumental for advancing integration into the EU. After the EU decision to invite Estonia to start accession negotiations, the issue has become not so much how sub-regional cooperation affects integration into the EU, but how the latter might affect the former. Lack of resources, most of which have been mobilized for EU oriented policies, has set further limits on intra-Baltic cooperation.

1.1.4. Therefore, the scope of intra-Baltic economic cooperation is influenced by how individual Baltic countries are situated in a gradual stage-by-stage process of integration into the EU. Participation in different stages might discourage further sub-regional cooperation.

1.1.5. Intra-Baltic market integration has been limited largely to negative measures. When harmonization was agreed, it has been based on references to the EU rules. Sub-regional rules, common economic policies and administrative structures have not been agreed upon because of coordination problems, high costs and unclear potential benefits.

1.2.1. The role of interest groups has increased with the advance of political and economic transition, although to a different extent in each of the three countries. Depending on the expected gains and losses resulting from market integration, some economic groups are likely to oppose sub-regional economic cooperation while others are likely to support it.

1.2.2. The enterprises using local resources and selling their goods domestically and domestically dominant (former state owned) enterprises have frequently demanded protection thereby negatively affecting intra-Baltic economic cooperation and market integration. Lack of resources for side payments to the disadvantaged groups has reduced the possibility for diminishing protectionist demands.

1.2.3. Protectionist demands are more likely to impede sub-regional cooperation when they exploit the opportunities offered by channels to the respective ministries or specialized agencies. The increasing complexity of regulation is likely to provide more opportunities for interest groups' demands to be met by governmental institutions. Adoption (or the prospect) of EU rules and policies can be used as a bargaining tool by the domestic groups.

1.2.4. The internationalization, or informal economic integration, of the intra-Baltic markets by increasing trade flows and the presence of foreign investors has exerted indirect pressure on formal cooperation. Increasing internationalization of activities is likely to stimulate demands for further abolishing non-tariff barriers to exchange and the movement of factors. However, the size of the intra-Baltic market and the characteristics of intra-Baltic trade, which limit the gains from economic cooperation, reduce incentives for strong demands.

The following sections discuss the development of intra-Baltic economic cooperation and the role of the above-identified factors. First, a brief description of intra-Baltic economic cooperation since the beginning of this decade is presented. The focus is on the trade agreements implemented as well as on those issues that Baltic governments failed to agree upon after bringing them on the agenda and specifying the deadlines, and on non-cooperative unilateral policy decisions. The next two sections examine the independent variables: the policies of the EU and the demands of economic groups. Finally, the conclusions and possible future developments are outlined.

IV. THE DYNAMICS OF INTRA-BALTIC ECONOMIC COOPERATION

The start of the period under analysis is the beginning of the decade when the Baltic States re-established statehood and began to conduct independent policies⁵⁴. Following the coordination of independence movements among the three countries, intra-Baltic cooperation has remained among the main priorities of their policies. Soon the first institutionalized setting for intra-Baltic

⁵⁴ The three countries declared independence in 1990: Lithuania on March 11, Estonia on March 30, Latvia on July 28.

cooperation was created which (as well as others that followed) was modeled on the Nordic cooperation institutions. The Baltic Assembly, made up of the representatives from the three legislative bodies of the Baltic States, was established on November 8, 1991. Six committees have been set up to discuss and suggest recommendations to the governments on the matters of common interest, including legal, social and economic affairs, environment and energy, communications, education and culture, and security and foreign affairs. The Baltic Assembly has been acting as the setting for exchange of information, discussions of the sub-regional issues, making declarations and drawing recommendations for the governments of the three countries. It meets twice a year on a rotating basis.

In September 1993, the agreement on creating the Council of Ministers was reached among the three Prime ministers, and on June 13, 1994, the Baltic Council of Ministers was established. Its tasks include taking decisions with regard to the recommendations of the Baltic Assembly, carrying out assignments in accordance with the intra-Baltic agreements concluded, and addressing matters of common interest. The Baltic Council of Ministers is chaired by the three prime ministers and conducts work on three levels: the ministers of foreign affairs, the Baltic cooperation Committee which coordinates activities of the Council between the meetings of the ministers, and the Committees of Senior Officials which cover about 20 issue areas and are permanent working bodies of the Council on a branch-ministerial level. Decisions of the Baltic Council of Ministers are made on the basis of consensus and are binding for the Baltic States except when they contradict the internal laws of each state and in such cases require approval by the state's legislative body⁵⁵. The Baltic Council established in April 1996, is a joint session of the Baltic Assembly and the Baltic Council of Ministers. The Baltic Council adopts declarations, and meets once a year. After setting up political institutions in the Baltic States and the elections of the presidents, summits of the three have also become a common practice.

In a few years, a dense network of coordination has been established among the Baltic States. Their work and impact have been highly dependent on the issue area and prospects for gains for each of the governments. Although intra-Baltic cooperative measures have been agreed and implemented in a number of areas, the discussion below is limited to policy measures related to sub-regional market integration and trade policy measures in particular⁵⁶.

⁵⁵ Lejins (1997:162-163).

⁵⁶ Environmental protection, transportation, and defense are examples of the areas where a number of common policy measures has been agreed upon. They all are characterized by negative or positive externalities which cooperative measures are targeted to reduce or increase. The most conflictual area has proved to be border issues: it took several years of

The idea of an intra-Baltic free trade area has been debated since the beginning of the decade (and long before). Like a number of other suggestions for intra-Baltic economic cooperation, this concept together with references to Benelux or other models has been brought up repeatedly by policymakers and analysts of the three states, however, without coming closer to a common agreement on its substance, form and implementation⁵⁷. The economic cooperation measures have been absent during the first years of the decade. The idea of a free trade area finally received strong political support during the meetings of Baltic heads of States in Jurmala (Latvia) in August 1993 when the draft of the free trade agreement was approved by the three and by the Prime Ministers in Tallinn in September 1993. This led to signing on September 13, 1993, of "the biggest agreement ever signed among the Baltic countries" – the intra-Baltic free trade agreement⁵⁸. Some analysts have characterized the agreement as a major "breakthrough in Baltic cooperation which, in the past, has often been nothing more than declarations with negligible practical effects"⁵⁹.

The free trade agreement signed in September 1993 excluded the agricultural goods. The agreement to abolish barriers to trade in this area has proved to be more difficult to achieve. After several rounds of intense negotiations, the agreement was finalized in June 1996 and came into force in January 1997. In November of the same year, the agreement on abolishing non-tariff barriers to trade was reached, and came into force in July 1998.

The analysis of cooperation dynamics comprises not only trilateral agreements reached but also failures to cooperate and non-cooperative decisions with regards to market integration. The failures to cooperate includes the customs union agreement that hasn't been implemented despite (and differently from other vague concepts of a "common Baltic economic area" or "common market") numerous pledges to do so and a concrete schedule being agreed upon. The other category includes unilateral protectionist measures that favor one country's domestic interests at the expense of other countries', and violate mutual commitments. These are briefly discussed next.

protracted negotiations between Estonia and Latvia to settle border dispute with the help of an external mediator, and the border between Latvia and Lithuania is still about to be settled. In both cases, the issue at stake is natural resources – fishing in the first, and oil in the second case.

⁵⁷ For example, the three states have signed the Agreement of Economic Cooperation in April 1990, and reached the agreement on establishing a customs union in September 1991. There have also been suggestions to establish a Baltic Investment Bank and a Baltic financial fund, coordinate monetary policy or even establish a currency union. None of these have been implemented. See Gricius (1994:26-32).

⁵⁸ Quotation from the speech of Latvian Prime Minister, cited in Gricius (1994:39).

⁵⁹ Gricius (1994:39).

Table 1. Intra-Baltic Market Integration Agreements

Agreement	Signed	In force	Main provisions	References to the EU
Free trade agreement	13.09.93	01.04.94	<p><i>Objectives:</i> to establish a free trade area in industrial goods (HS 25-97); to promote mutual trade, productivity and economic growth; guarantee fair competition; to promote development of trade in the Baltic sea area; to encourage cooperation in other economic areas.</p> <p><i>Measures:</i> the elimination of all export and import duties with several exceptions relating to export restrictions; a standstill clause on qualitative export or import restrictions; elimination of quantitative restrictions with some exceptions; non-discrimination and national status principles; special provisions relating to restructuring.</p> <p><i>Rules of origin and safeguards:</i> Baltic origin cumulation; general GATT based safeguards</p> <p><i>Dispute settlement mechanism:</i> Joint Committee to oversee the implementation of the agreement, settle disputes, to provide a setting for exchange of information and consultations.</p>	The parties see the agreement as a means to reinforce participation in European economic integration (preamble)
Agreement on free trade in agricultural goods	16.06.96	01.01.97	<p><i>Objectives:</i> to establish a free trade area in agricultural, food and fisheries products (HS 01-24); to promote development of mutual trade and fair competition.</p> <p><i>Measures:</i> the elimination of export and import duties and quantitative restrictions; a standstill clause; non-discrimination and national status principles</p> <p><i>Rules of origin and safeguards:</i> Baltic origin cumulation; general GATT based safeguards</p> <p><i>Dispute settlement mechanism:</i> Joint committee created under the previous agreement</p>	The parties declare their intention to participate in European integration processes, and the agreement is to promote this objective (preamble)
Agreement on abolishing non-tariff barriers	20.11.97	01.07.98	<p><i>Objectives:</i> to abolish non-tariff barriers to trade; develop a free trade area.</p> <p><i>Measures:</i> the mutual recognition of sanitary, phytosanitary and technical standards applied to products and production processes (HS 01-97); harmonization in line with EU and other relevant international institutions' rules; a standstill clause; non-discrimination and national status principles; establishment of Information center</p> <p><i>Rules of origin:</i> Baltic origin cumulation.</p> <p><i>Dispute settlement mechanism:</i> Joint Committee to oversee the implementation of the agreement, settle disputes, to provide a setting for exchange of information and consultations.</p>	The final objective of EU membership acknowledged; the intra-Baltic cooperation and integration into the EU should proceed in parallel (preamble). EU rules on product and process standards form a basis for mutual recognition and work of local certification agencies

Source: Respective trilateral trade agreements

The idea of creating an intra-Baltic customs union was discussed at the governmental level in Tallinn in April 1991. During the meeting of the three governments in September 1991, a statement "On Establishment of a Customs Union on the territory of Estonia, Latvia and Lithuania" was issued. This

question was repeatedly discussed at the level of countries' policy-makers and senior officials during the following years⁶⁰. However, no cooperative measures were implemented in this field. The efforts were revived with the resolution on the establishment of a customs union signed by the Prime Ministers of the three countries in February 1995. The deadline of 1998 was set up for establishing the intra-Baltic customs union. Another impetus was given by signing the agreement to lift tariff measures to trade in agricultural goods. More specific steps were further elaborated in another resolution signed by the Prime ministers in February 1997. The commitment to create a customs union in 1998 was reiterated again during the signing of the agreement on abolishing non-tariff barriers in November 1997. However, the intra-Baltic customs union has not been created, and it is not likely to be in the future.

On the contrary, the autumn of 1998 saw a number of beggar-thy-neighbor measures introduced by the three countries in a series of retaliation steps. First, the possibility of reintroducing trade protection measures in the area of agricultural trade was discussed in a joint meeting of the three ministers of agriculture in September. Despite the protests of the other countries, at the end of 1998 the Latvian government presented the Parliament a proposal to introduce quotas for meat exports from Estonia and Lithuania. This was rejected in the beginning of 1999 in the face of increasing protests from Estonia and Lithuania as well as some international institutions. In October and November, Lithuania and Estonia introduced protectionist measures against exports of meat products from each other's market following an exchange of allegations that these products did not conform to veterinary standards. The "pork war" was ended in December⁶¹. In the beginning of 1999, intra-Baltic free trade was again distorted by disagreements between Latvia and Lithuania concerning rules of origin and between Lithuania and the other two countries concerning the rules of customs valuations applied by Lithuania⁶². Mutual accusations of breaking the rules of free trade agreements were exchanged, and retaliatory measures threatened. Although during the meeting in Vilnius in January 1999, Prime ministers of the Baltic States agreed to remove the obstacles to trade, the tensions have continued, and the Latvian government started preparing a project to restrict the import of eggs from Lithuania⁶³. On March 17, the Latvian veterinary institution announced the restrictions on some exports from Lithuania. In a trilateral meeting several days later the implementation of protectionist measures was denied. In March, the Estonian government accused Lithuania of discriminatory rules of providing subsidies and purchasing pork.

⁶⁰ For example, there were four meetings of Baltic States' customs officials. (Gricius 1994:35).

⁶¹ The Baltic Times, December 3-9, 1998, "Baltics want end to pork war", p. 14.

⁶² Lietuvos Rytas daily, January 28, 1998, www.lrytas.lt/19990128/eko28ati.htm

⁶³ Lietuvos Rytas daily, February 25, 1999, www.lrytas.lt/19990225/eko251vb.htm

Finally, in June Latvia introduced temporary import tariffs on pork imported from Estonia and Lithuania. The latter threatened to retaliate but import tariffs remained in place. As it will be discussed later, most of the protectionist measures following the economic crisis and the resulting fall of demand in Russia have been initiated by the demands of local interest groups.

V. THE EU AND INTRA-BALTIC ECONOMIC COOPERATION

A. The Period of Uncertainty

The first years of relations between the EC/EU and the Baltic countries have been marked by a group approach taken by the EC/EU towards the three. Although EC/EU conducted negotiations with each Baltic State bilaterally, general policy ranging from the establishment of diplomatic relations to the initiation of individual trade agreements had a strong group or "Baltic sub-region" emphasis. The group approach towards the Baltic States was reinforced by support of intra-Baltic cooperation measures which EU representatives have encouraged on various occasions directly and indirectly by urging the strengthening of economic cooperation among transition countries in general. The economic cooperation of the Visegrad countries, and the EU statements that economic integration among transition countries should proceed in parallel with their integration into the EU, have provided a reference model to be followed for the Baltic States' policy makers. Once the prospects of integration into the EU became more certain, and the Baltic States' leaders realized that intra-Baltic economic cooperation was likely to maximize their chances of integration into the EU, they were willing and able to proceed with sub-regional cooperation. These developments are discussed below.

The EC recognized the independence of the three Baltic States in August 27, 1991, and in April 1992 the ambassador of the EU to the Baltic States started his activities⁶⁴. In the meeting with the foreign ministers of the Baltic States at the beginning of September, EC representatives suggested including the three states into the Phare program, thereby differentiating them from the other former Soviet Union republics, as well as starting to prepare trade and cooperation agreements similar to those concluded with CEECs. The subject of intra-Baltic cooperation, particularly in the field of external relations in the context of developing their relations with industrialized countries and the EC, was voiced during the visit of the Commission vice president Andriessen⁶⁵. In September 1991, negotiations of the "first generation" trade and cooperation agreements started. The agreements were signed in May 1992 and came into force in the

⁶⁴ Prikulis (1994:93).

⁶⁵ Bulletin of the EC, no. 9, 1991, p. 44.

first months of 1993. The agreements were supplied by the EU and their enforcement has upgraded the trading status of the Baltic States in the general "pyramid of preferences" of the EU by extending Most Favorite Nation status and Generalized System of Preferences as well as abolishing specific import restrictions previously applied to the state-trading economies (see Annex 1).

Already during the negotiations of the trade and cooperation agreements the representatives of the Baltic States raised the issue of association with the EU. Their aim was to conclude association agreements similar to the ones signed by the EU with the Visegrad countries, and thereby to be included in the group that, after a period of hesitation among the EU leaders, was recognized as a group of prospective EU members. This hope was expressed by the foreign ministers of the Baltic countries when the trade and cooperation agreements were signed in May 1992. The Estonian foreign minister, J. Manitski, called the accords "our first step back to Europe", which he hoped would lead to full EC membership within a few years⁶⁶. The recognition that these agreements could lead to association was also included in the preambles of the agreements. The Baltic States again expressed their wish to join the EU in the conference of 64 countries on aid to the former Soviet Union in Lisbon at the end of May 1992⁶⁷. The negotiations of the Europe agreements and eventual EU membership has moved to the top of the agendas of the Baltic governments. However, the attitude of EU policy-makers was rather reserved. The emphasis of EU leaders expressed by the President of the Council, Pinheiro, during the meeting in Lisbon, and reiterated in its conclusions, was on the importance of regional cooperation among the "new independent states"⁶⁸. The question of development of the EU's relations towards the Baltic States was not addressed. Later various proposals about possible forms of economic and political links with the Baltic States were debated, illustrating uncertainty about whether they can be included into the category of potential members⁶⁹. The prospect of the eventual membership was quite uncertain at the best.

Despite the uncertainty concerning the further development of relations with the Baltic countries, the EU assumed a leading role in supporting economic and political reforms in these countries. The technical assistance program of Phare was extended to the Baltic States. The EU Commission acted in close coordination with international financial institutions, for example making aid

⁶⁶ The Baltic Independent, May 15-21, 1992, "Baltics sign trade deals with EC", p. 4.

⁶⁷ The Baltic Independent, May 29 - June 4, 1992, "Baltics want triangular trade", p.1.

⁶⁸ Bulletin of the EC, no. 5, 1992, p. 80.

⁶⁹ As it was observed about the EC/EU's response to the developments in the CEECs, the resulting policy constituted 'a curious mix of tradition and innovation' (Sedelmeier, Wallace 1996:355), and 'more a conglomeration of discrete activities than the result of a well-developed coherent strategy' (Kramer 1993:221).

conditional upon the adoption of the IMF economic recovery programs. Part of Phare funds and technical assistance measures were directed towards facilitating economic liberalization and supporting economic cooperation by improving the administration of trade and supporting the development of exports. Trade liberalization and sub-regional cooperation among the transition economies was encouraged as a part of the general support for economic transformation and democratic consolidation⁷⁰.

A group approach towards the Baltic States was reinforced by the support of intra-Baltic cooperation measures which EU representatives have encouraged on various occasions. During the meeting at the beginning of July 1992, G-7 leaders urged "all CEECs to develop economic relations with each other"⁷¹. This was directed in particular towards the Visegrad countries. In their case the link between sub-regional economic cooperation and integration into the EU has been very explicit. The Visegrad countries decided to create a free trade area only after signing the Europe agreements with the EU, and tuned sub-regional trade barriers' reductions to those with the EC⁷². Sub-regional integration among the Visegrad countries was strongly welcomed by the EC⁷³. At the same time, "the Visegrad example" provided a model that the Baltic States could follow.

The EU's policy towards the Baltic States has been conducted using other regional institutions, in particular the Council of the Baltic Sea States (CBSS). The CBSS was created in 1992 in Copenhagen, where 10 countries and the Commission of the EU were represented. It has become an important institution for the development of ties between the Baltic States and the EU, and for the EU's support of sub-regional cooperation. Its importance was underlined by the fact that it included Germany, Denmark and the future Nordic members of the EU that have become the main supporters of Baltic States' integration into the EU⁷⁴. "The Baltic Sea dimension" of EU's policy was strengthened further after Sweden and Finland became members of the EU in 1995.

The situation in the Baltic States during the first years of transition was characterized by radical political and economic institutional changes, which imposed constraints on intra-Baltic economic cooperation. As the policy makers

⁷⁰ Although some observers have concluded that the emphasis on sub-regional cooperation reflected a lack of a clear strategy on the part of the EU with which to respond to the urgent needs of the region (see Inotai 1997:15).

⁷¹ Bulletin of the EC, no. 7/8, 1992, p. 142.

⁷² Hoen (1998:39).

⁷³ Bulletin of the EC, no. 10, 1992, p. 128.

⁷⁴ Already during the founding meeting of the CBSS German Foreign minister H.D. Genscher declared that the Baltic states "must be offered association accords with the EU similar to those signed with Poland, Czechoslovakia and Hungary" (The Baltic Independent, March 13-19, 1992, "Baltic region forms council to build democracy and speed growth", p. 5)

of one Baltic State acknowledged at that time, "the tense domestic situation" rendered advancing sub-regional cooperation impossible⁷⁵. Uncertainty and a lack of resources has limited the ability of governments to implement sub-regional cooperation schemes. The work of the already established intra-Baltic institution – the Baltic Assembly – has been hampered by the lack of financial resources, while the level of expertise for designing sub-regional market integration schemes was low⁷⁶. This was a period of learning and a mixture of institutional imitation and innovation. Absence of a regional coordinator and supplier of cooperation rules made commonly acceptable agreement on the form and substance of economic cooperation more complicated, although various proposals, often based on references to the Benelux or other models, were discussed (see section IV).

The Baltic States established foreign trade regimes in 1992 and 1993, ranging from a very liberal one applied by Estonia to more protectionist ones, particularly in the trade of agricultural goods, applied by Latvia and Lithuania. The introduction of market institutions, and, for example, national currencies created the necessary basis for sub-regional economic cooperation, although different levels of progress in each of the three states has posed temporary limits. Estonian officials have referred to the slow progress of the Lithuanian side in introducing the national currency and in instituting a visa regime for CIS nationals, as an obstacle for a trilateral trade agreement⁷⁷. Willingness to proceed with trilateral economic cooperation on the Estonian side has also been temporarily decreased by the formation of a left wing government in Lithuania as a result of "a protest vote" during the elections in Autumn of 1992. Estonian right wing government officials have been quoted as referring to "the anti-business policies" of the new Lithuanian government, and therefore have been considering the conclusion of a bilateral free trade agreement with Latvia instead⁷⁸. These differences, however, proved to have only a temporary effect on intra-Baltic relations.

Prospects for intra-Baltic economic cooperation started changing in 1993, and the major push to advance it is attributed to EU policies. The first indication of changing EU policy towards the Baltic States - not without the major efforts

⁷⁵ The Baltic Independent June 5-11, 1992, "New strains on Baltic unity", p. 1.

⁷⁶ Notably, Nordic diplomats have been reported to have expressed dissatisfaction with the level of preparation on the Baltic States part during the signing of Nordic and Baltic States cooperation agreement 1992 (The Baltic Independent June 5-11, 1992, "New strains on Baltic unity", p. 1).

⁷⁷ The Baltic Independent, August 20-26, 1993, "Lithuania seeks to join Baltic trade deal", p. 1.

⁷⁸ Estonia has even been voicing doubts about the necessity of the Baltic Assembly (The Baltic Independent, April 2-8, 1992, "Trade row highlights north-south gap", p. 1.; Jurgaitiene and Waever (1996:213)).

of the Danish government - was an invitation to participate in the conference organized in Copenhagen in April 13-14, 1993. The conference gathered representatives from the EU, EFTA and CEECs to discuss matters of European integration, and the final declaration acknowledged the aim of several participating countries (meaning the Baltic States) to become the members of the EU⁷⁹. The following months were characterized by the initiatives on the part of the EU and response of the Baltic States which led to the intra-Baltic free trade agreement. Several days after the conference, the EU troika and Commissioner Van den Broek had a meeting with the Foreign ministers of the Baltic States during which issues of EU relations with the three and economic liberalization and cooperation within the Baltic region were discussed⁸⁰. The Baltic States' representatives raised the issue of establishing a free trade area with the EU. However, the response from the EU, namely Belgian Foreign minister Claes, was that the three "should first improve cooperation among themselves"⁸¹. He also indicated that the Baltic States could learn from the Benelux example.

Before going to the meeting with EU representatives, the Prime Ministers of the Baltic States met in Vilnius to discuss their relations and common position towards the EU⁸². The Baltic States leaders have met again at the beginning of June, before the EU summit in Copenhagen, and issued a joint document urging the EU to begin talks on association with the Baltic States⁸³. Although the EU Summit in June 21-22 did not recommend starting association negotiations, the decision to ask the Commission to develop proposals on free trade agreements with the Baltic States marked a step towards integration of the three into the EU. The conclusions of the Copenhagen Summit also stated that accelerated opening of EU markets to the transition countries is expected "to go hand in hand with further development of trade between those countries themselves"⁸⁴. The same attitude was again expressed during the meeting of G-7 leaders in Tokyo in July, who urged "stronger cooperation among the countries in transition themselves"⁸⁵.

These decisions have strengthened the perception of the Baltic States' governments that their major objective – integration into the EU – is likely to be facilitated by sub-regional cooperation. This was very explicitly stated by the leaders of the three countries during the meeting in Jurmala, in August 1993,

⁷⁹ Martikonis (1997:8).

⁸⁰ Bulletin of the EC, no. 4, 1993, p. 54.

⁸¹ Cited in Arnsfeldt (1998:50).

⁸² The Baltic Review, vol. 2., no. 2, March – June 1993, "Politics or Economics", p. 9.

⁸³ Prikulis (1994:106).

⁸⁴ Bulletin of the EC, no. 6, 1993, p. 13.

⁸⁵ Bulletin of the EC, no. 7/8, 1993, p. 130.

when the three presidents jointly declared their intention to integrate into the EU, and that the aim to achieve Baltic integration was a step towards integrating the sub-region with the EU⁸⁶. The intra-Baltic free trade agreement was signed in September 13. It was modeled on the bilateral free trade agreements that the Baltic States concluded about a year ago with some EFTA countries. The intention to proceed further by liberalizing trade in agricultural products was indicated in the preamble of the agreement.

The conclusion of the agreement was declared to be a major step towards the integration of the three into the EU. The intra-Baltic free trade agreement was clearly perceived by the Baltic States' leaders as maximizing their chances to integrate into the EU. As Estonian President Lenart Meri remarked, "we can't reenter Europe through three doors and then get together there"⁸⁷. The instrumental value of the agreements was reaffirmed again during the meeting of the Foreign Affairs ministers of the three states in December, following the decision of the Commission to start discussions on Baltic free trade agreements. The ministers have jointly appealed for prompt ratification of the intra-Baltic free trade agreement, and declared that this "would pave the way for more lucrative treaties with the EU in the immediate future"⁸⁸.

The intra-Baltic free trade agreement was positively evaluated by the EU Commission which was at the time preparing bilateral free trade agreements with the Baltic States. A memorandum on the free trade agreement between the EU and Latvia prepared in September stated that the intra-Baltic free trade agreement, which provided for integration among the three, would assist in their future integration into the EU⁸⁹. The preparation for talks on the Baltic States' free trade agreements with the EU took place in the second half of 1993. At the beginning of December, the Commission presented the Council its recommendations to negotiate free trade agreements with the three "taking into account specific features" of the Baltic countries. The latter qualification probably referred to the still unclear policy concerning the possible accession of these countries. The Commission also noted that the conclusion of the free trade agreements would ensure that existing agreements between the Baltic States and Nordic countries will be compatible with EU's *acquis* after the accession of the latter.

⁸⁶ Prikulis (1994:106).

⁸⁷ The Baltic Independent, September, 3-9, 1993, "Baltic leaders give a new lease of life to co-operation", p. 1

⁸⁸ The Baltic Independent, December 10-16, 1993, "Foreign ministers rebuke Russia on "peacekeeping forays", p. 1.

⁸⁹ Prikulis (1994:107).

On February 7, 1994, the EU Council confirmed the Commission's mandate to negotiate free trade agreements with the Baltic countries. The Council and the Commission issued a declaration, which acknowledged the importance of further strengthening integration between the Baltic States and the EU and declared that the free trade agreements would constitute an important step to this end. The declaration also stated that "the Council will take all necessary steps with the aim of negotiating and concluding Europe agreements as soon as possible in recognition of the fact that Estonia, Latvia and Lithuania are to become members of the EU through the Europe Agreements"⁹⁰. Thus, the EU explicitly acknowledged the aim of the Baltic States to become EU members. Although the Europe Agreements were to become the main instruments of integration, the strategy of integration was still uncertain.

In the following months, the bilateral negotiations of the free trade agreements between the EU and the Baltic States took place. The three agreements were signed in July 18, 1994, and came into force in January 1995. The agreements supplied by the EU and modeled on interim agreements concluded before with other CEECs have resulted in different provisions concerning the speed and scope of liberalization. Their content have been comparatively analyzed elsewhere, therefore it suffices to point out several features relevant to this analysis⁹¹. First, the agreements explicitly recognized the need for continuing intra-Baltic cooperation, taking into account that closer integration between the EU and the Baltic States, and the Baltic States themselves should proceed in parallel⁹². Second, the provisions of the agreements to a certain extent reflected differences in the economic policies in each of the Baltic States which were conditioned by domestic political economy processes (see section VI).

These developments have spilled-over into other areas of Baltic economic cooperation. The intensified intra-Baltic cooperation resulting from EU policies towards the three has expressed itself in the decision of March 1994 to extend the sub-regional free trade area to the Visegrad countries, and in the establishment of the Baltic Council of Ministers in June 1994, and a couple of months later the Secretariat of the Baltic Council of Ministers⁹³. Joint Baltic

⁹⁰ Bulletin of the EU, no. 1/2, 1994, p. 73.

⁹¹ For example, Estonia has committed itself to free trade without a transitional period, Latvia has negotiated 4 years and Lithuania - 6 years transitional periods to gradually remove trade restrictions. For a legal analysis of these agreements see Peers (1995), for an economic analysis, see Sorsa (1997).

⁹² Preamble of the free trade agreement between the EU and Lithuania.

⁹³ As the Prime minister of Estonia has noted during the opening of the Secretariat, "as we all move towards the EU we have to prove our capacity to integrate between ourselves" (The Baltic Independent, September 16-22, 1994, "New Baltic structure opens in Riga", p. 1).

projects in infrastructure financed by the EU have been agreed. However, earlier announced plans to extend the intra-Baltic free trade regime to agricultural goods and proceed with the establishment of an intra-Baltic customs union have been stalled. For some time, the Baltic States have been actively involved in relations with the EU, which has declared the Baltic region a "major focus" of its external policy⁹⁴. At the same time, the political economy forces have impeded further developments in intra-Baltic economic cooperation.

B. Pre-accession and the Development of the Group Approach

In the 1994-1996 period, the EU continued its group approach in bilateral relations with the Baltic States, although it has gradually shifted its emphasis to the individual progress of each applicant in terms of future accession to the EU. The EU decided to start negotiating the Europe Agreements with the three even before the free trade agreements came into force. In August 1994, negotiations were opened simultaneously with the three countries. Although they were conducted bilaterally, the agreements were all signed on June 12, 1995. They have incorporated the free trade agreements, and added new dimensions to the Baltic States' relations with the EU including political dialogue and economic cooperation in a number of areas, and approximation of laws to the EU's *acquis*.

The Europe Agreements have marked a new stage of Baltic States' integration into the EU and upgraded their status to that of other associated countries⁹⁵. The agreements came into force only in February 1998, after the Baltic States' parliaments, EU member states' parliaments, and the European Parliament ratified them. However, already before their conclusion, the EU has decided that after the Europe agreements are signed, these countries could be included in the pre-accession strategy⁹⁶. The Baltic States were invited to the Cannes summit in June 1995, where the EU confirmed that the Baltic States can be included into the strategy to prepare for accession defined in Essen⁹⁷. The pre-accession strategy included such instruments of integration as Europe Agreements, Phare, the structured relationship between the CEECs and the EU, and the White paper on integration into the internal market (see Annex 1). In other words, the Baltic States were provided with the opportunity to further integrate their markets into the EU, participate in the Council meetings together with other CEECs, and to focus on adopting EU's legal rules governing the

⁹⁴ EU Commissioner Brittan quoted in *The Baltic Independent*, May 27 – June 2, 1994, "Summit pledges European ties", p. 2.

⁹⁵ Lithuania's Prime minister Slezevicius has been quoted as saying that "Europe agreement, no doubt, is the most significant Lithuanian international agreement this century" (*The Baltic Independent*, June 16-22, 1995, "Baltic states re-enter Europe", p. 1).

⁹⁶ See the Conclusions of the Essen summit (*Bulletin of the EU*, no. 12, 1994).

⁹⁷ See the Conclusions of the Cannes summit (*Bulletin of the EU*, no. 6, 1995).

internal market. In the latter case, the Commission has suggested that each country should draw up its own timetable of legal approximation.

In parallel, the EU was using every opportunity to stress the need for advancing sub-regional cooperation. For instance, during the visit of Commission representatives to the Baltic States to discuss the Europe Agreements, they indicated that "it could only be in the Balts' interest to cooperate closely with each other"⁹⁸. The preambles of the Europe Agreements have included the recognition of "the need for continuing regional cooperation among the Baltic States"⁹⁹. Similar statements were repeated by representatives of the other EU institutions. In January 1995, a delegation from the European parliament called for greater intra-Baltic cooperation stressing the importance of free trade among the Baltic States¹⁰⁰. In May 1996, the president of the European Parliament suggested during his speech to the Estonian parliament that the Baltic countries should "cooperate more closely in order to better their chances of EU membership"¹⁰¹.

These statements represented a shift from *ad hoc* encouragement to a more coherent EU policy towards sub-regional economic cooperation in the CEECs. This policy has been most explicitly presented in the Essen summit conclusions, which stated that "being aware of the role of regional cooperation within the Union, the Heads of State or Government emphasize the importance of similar cooperation between the associated countries for the promotion of economic development..."¹⁰². This statement was included in the section on the accession preparation strategy and formed a part of it, allowing some analysts to conclude that intra-regional cooperation has come to be seen as a requirement for EU membership¹⁰³.

The EU's policy of support for intra-Baltic economic cooperation found its expression and was constantly reaffirmed in a more general framework of EU policy towards the Baltic Sea region. As was mentioned before, in 1994 the Baltic Sea region was declared to be a major focus of its external policy. On October 24, 1994, the Council adopted the Communication on Orientation for a Union Approach towards the Baltic Sea region presented by the Commission. It

⁹⁸ The Baltic Independent, August 5-11, 1994, "Way cleared for Baltic negotiations with EU", p. 2.

⁹⁹ Preamble to the Europe agreement between the EU and Lithuania.

¹⁰⁰ The Baltic Independent, January 13-19, 1995, "Euro-MPs call for Baltic integration", p. 4.

¹⁰¹ This referred in particular to the border disputes among the Baltic States (The Baltic Independent, May 9-15, 1996, "Haench: settle quarrels, then think about EU", p. 4.).

¹⁰² Bulletin of the EU, no. 12, 1994, p. 13.

¹⁰³ Maresceau (1997:9). Although the importance attached by the EU to the intra-regional cooperation was largely motivated by security reasons, economic cooperation was seen as an important part of it.

acknowledged that “the forthcoming enlargement of the EU and the move towards closer relations with the countries of the Baltic create a need for an overall Union policy for that region”¹⁰⁴. The EU’s approach was based on the regional dimension of cooperation and among other things supported greater cohesion between existing regional initiatives and cooperation in trade and economic matters. It also foresaw the financing of regional projects such as infrastructure, under the Phare framework.

On May 29, 1995, the Council adopted the conclusions on EU policy towards the Baltic Sea region, and reaffirmed its policy targeted to promote “initiatives to expand trade between Baltic Sea States which are not members of the Union by providing suitable assistance, e.g. in the customs field”¹⁰⁵. The Council also asked the Commission to prepare a report on the current state of and perspectives for the cooperation in the Baltic Sea region. At the end of November, 1995, the Commission presented the report in which financial contributions from the EU and other institutions and countries provided during the first half of the decade to the Baltic Sea region were assessed and future projections presented¹⁰⁶. According to the Commission, over the period of 1990-1994 a total of 206 MECU were provided to the Baltic States in the context of national Phare programs, most of which concentrated on economic stabilization and restructuring. Multi-annual Indicative Programs for the period 1995-1999, covering an estimated total of 430 MECU, were under preparation for the three countries¹⁰⁷. These measures were expected to focus on pre-accession, medium-term restructuring, infrastructure investment and regional cooperation. The Commission concluded that “the scope for the development of such a specifically regional Union approach to the countries of the Baltic Sea region exists, based upon a deepening of the Union’s own bilateral relationships and supported by the active encouragement and support of inter-regional and sub-regional cooperation”¹⁰⁸.

In December 1995, the EU’s leaders asked the Commission to propose “a suitable regional cooperation initiative” to be presented during the conference of the Council of Baltic Sea States scheduled for May 3-4, 1996¹⁰⁹. Following this decision, the Commission adopted a Communication on a regional cooperation

¹⁰⁴ Bulletin of the EU, no. 10, 1994, p. 53-54. The communication was adopted the same day when the Commission has recommended the Council to authorize negotiations of the Europe agreements with the Baltic States.

¹⁰⁵ Bulletin of the EU, no. 5, 1995, p. 66.

¹⁰⁶ See Commission (1995).

¹⁰⁷ Commission (1995:3-4). Statistics of financial support provided to each of the Baltic States bilaterally by EU members and Nordic countries illustrated quite clearly the priorities of different countries.

¹⁰⁸ Commission (1995:1).

¹⁰⁹ Bulletin of the EU, no. 12, 1995, p. 96.

initiative in the Baltic Sea region in April 10, 1996. It proposed “strengthening democracy, political stability and economic development in this region ... by taking full advantage of existing cooperation instruments”, and fostering regional cooperation¹¹⁰. This implied not only support for cooperation in the whole region but also for the sub-regional arrangements such as the intra-Baltic economic cooperation schemes. The position of the EU was then presented at the Visby meeting of the Council of the Baltic Sea States on May 3-4, 1996, which was attended by the President of the Council and the President of the Commission. The declaration adopted in Visby called for more cooperation in several areas including economic development and integration, and stressed its support for the “early realization of a free trade area between Estonia, Latvia and Lithuania”¹¹¹.

Thus, the EU has gradually developed a policy towards sub-regional cooperation, and intra-Baltic economic cooperation in particular, which consisted of (1) general support for intra-regional economic cooperation measures as an element of economic transition, (2) an emphasis on sub-regional cooperation as an element of preparation for accession, (3) the supply of rules for sub-regional cooperation based on the EU’s integration record, (4) financial support for sub-regional initiatives. It should be noted that financial support was targeted towards improvement of administrative capabilities, fostering exports and, increasingly, pre-accession measures. For rather obvious reasons it was not provided for redistribution purposes and side-payments for groups facing adjustment pressure resulting from liberalization and market integration as has been practiced inside the EU. Leaving aside the issues of sufficiency, efficiency and necessity of concrete support measures, the EU’s policy of support for intra-Baltic cooperation schemes backed by the supply of rules and some resources seems to have played a major role in advancing intra-Baltic economic cooperation *insofar as* it was perceived by the Baltic States’ leaders as maximizing the chances of integration of their countries into the EU.

After signing the free trade agreement in 1993, plans for extending the scope of intra-Baltic market integration and common trade policies have remained in the preparatory stage for several years. Support for extending the scope of intra-Baltic economic cooperation was frequently expressed by the leaders of the three states. For example, the meeting of the three Prime ministers on February 13, 1995 set a target for intra-Baltic customs union, which was agreed to enter into force from January 1, 1998. Free trade in agricultural products was also discussed with Estonian representatives stressing the difficulty of aligning their liberal agricultural trade policy with the other two

¹¹⁰ Bulletin of the EU, no. 4, 1996, p. 69.

¹¹¹ The Baltic Review, Summer 1996, vol. 10, “The Visby Summit: Baltic Europe and EU”, p. 3.

states that were more protectionist¹¹². These differences have become apparent also during the negotiations of bilateral agreements between each of the three Baltic States and the EU. As will be discussed in the next section, divergent preferences of the three governments have been largely determined by domestic political economy forces. Therefore despite constant EU support for intra-Baltic economic cooperation, the next measure extending the scope of intra-Baltic market integration was agreed only in June 1996, after the change in the government in Latvia.

The intra-Baltic agreement on free trade in agricultural goods was signed on June 16, 1996, after several months of negotiations. It came into force at the beginning of 1997. The preamble of the agreement stated the intention of the three states to participate in the European integration process and the agreement was seen as a way towards meeting this objective. It was reported that the agreement was drafted taking into account the goal of Baltic States to join the EU¹¹³. The significance of the agreement as an instrument towards the integration of the three into the EU was stressed by the three Baltic States' presidents in Vilnius at the end of May, after the text of the agreement was finalized. The joint declaration of the three presidents stated that the creation of a free trade area for agricultural products would create "an important precondition for integration of the Baltic States into the EU internal market"¹¹⁴. The following agreement on extending the scope of intra-Baltic economic cooperation – this time in the area of non-tariff barriers – was taken after more than a year. This period was marked by changes in individual integration of the Baltic States into the EU, which impacted on further dynamics of intra-Baltic economic cooperation.

C. Differentiation and Accession Negotiations

Change in EU policy towards the Baltic States (and the applicant countries in Central and Eastern Europe in general) became apparent with the announcement of the Commission's Opinions on the applicant countries in July 1997. The group approach was abandoned in favor of an individual approach towards integration of the applicant countries into the EU. Although the proposal to start accession negotiations with some countries, and not the others has created new groups of "ins" and "pre-ins", to use the terminology of the Commission, the result in the case of the Baltic States was their differentiation. This change of EU policy has caused a change in intra-Baltic relations, although the EU continued emphasizing the importance of sub-regional cooperation. However,

¹¹² The Baltic Independent, February 17-23, 1995, "Despite customs plans, tone of PM summit is subdued", p. 1.

¹¹³ Together in Europe, No. 90, June 1, 1996, p. 3.

¹¹⁴ Cited in Agence Europe, Brussels, 30.05.1996.

the potential benefits of intra-Baltic economic cooperation as a means of maximizing the chances of EU membership for some of Baltic States' governments, the Estonian in particular, decreased, and incentives for other targets of cooperative efforts were strengthened.

The signs of changing EU policy towards the prospective members appeared before the presentation of the Opinions. The Copenhagen accession criteria represented a major shift in the Union's policy of integrating candidate countries into the EU. The definition of membership criteria, however vague and broad, have for the first time indicated that every country would be assessed in terms of its development and ability to meet the criteria. At that time the concrete strategy of integration, especially in the case of the Baltic countries, was far from clear. The EU was constantly encouraging sub-regional cooperation as a way to prepare for accession (or as a sign of a clear integration strategy, depending on one's view). With the prospect of membership negotiations becoming clearer, the emphasis, however, gradually shifted from the group approach towards individual preparedness for accession. In November 1995, the Commission presented its interim report on the effects of EU enlargement on its policies where it was stressed that the countries "will accede on an individual basis in the light of their economic and political preparedness and on the basis of the Commission's opinion on each applicant"¹¹⁵. This approach was confirmed in 1995 Madrid summit of the EU, which decided that each country was to be treated separately. The Madrid Council also asked the Commission to "expedite preparation of its opinions on the applications made so that they can be forwarded to the Council as soon as possible after the conclusion of the intergovernmental conference"¹¹⁶. By that time, all three Baltic States have had their membership applications presented to the EU¹¹⁷. Early in 1996, the Commission started collecting necessary information for preparing the Opinions, which were to assess the state of the applicant countries on the basis of the membership criteria. The Opinions were presented in July 1997, and recommended opening accession negotiations with Estonia, among other countries, but not with Latvia and Lithuania. After intense debates inside the EU during the second half of 1997, the European Council in Luxembourg confirmed the differentiation of the applicant countries, although in a somewhat "softer" form of "ins" and "pre-ins" and new multilateral arrangements including all

¹¹⁵ Bulletin of the EU, no. 11, 1995, p. 69.

¹¹⁶ Bulletin of the EU, no. 12, 1995, p. 18.

¹¹⁷ Latvia applied on October 10, 1995, Estonia – on November 24, 1995, Lithuania – on December 8, 1995. In general the timing was related to the forthcoming EU summit in Madrid, although in case of Latvia domestic situation also has played a role.

candidates"¹¹⁸. At the same time, the Council declared that "each of the applicant states will proceed at its own rate, depending on its degree of preparedness"¹¹⁹.

The ambiguity of the EU group approach during the period leading to the explicit differentiation of the Baltic States in 1997 was reflected in the attitudes of Baltic States' policy makers in assessing to what extent "preparedness" of their countries for accession could be advanced by intra-Baltic cooperation. This was in particular evident in Estonia's policy. As early as November 1994, the Foreign Minister of Estonia declared during the conference organized in Tallinn, that Estonia prefers admission to be decided on the basis of "individual countries rather than groups", and "should any of the Baltic States meet the admission criteria, its admission should proceed immediately"¹²⁰. Similar statements were issued in 1995 and 1996, although usually followed by joint declarations of the Baltic States' leaders that the accession negotiations should be started at the same time with all three Baltic countries. An example of such an ambiguous policy was the statement made by Estonian President L. Meri in March 1996, during his visit to the Commission that "each of the applicant countries must be dealt with separately, namely, on its own merits"¹²¹. This statement caused criticism from the other Baltic States, and in particular, Lithuania, and several months later the Presidents of the three countries have declared that the three countries are going to integrate into the EU together, "making the show of their common front" as some have commented¹²². In October 1996, the Estonian president reaffirmed his support for an intra-Baltic customs union during the meeting with the Latvian President in Riga¹²³. The ambiguity of Estonia's policy towards intra-Baltic cooperation was also reflected in negotiations of the bilateral free trade agreements with the EU, which the EU and the Baltic Assembly encouraged to coordinate with the other two Baltic countries. The Estonian attitude was expressed by the statement of an official from the Ministry of Foreign Affairs who stated "had we agreed [to coordinate negotiations] it would have been like we had bombs tied to our feet, waiting until others catch up"¹²⁴. However, before the actual differentiation of the Baltic States, intra-Baltic economic cooperation was perceived in all three countries as an important instrument for individual integration into the EU, especially against the background of intensive support for sub-regional cooperation expressed by the

¹¹⁸ For reactions of the member states and applicant countries to the Commission's Opinions see Avery and Cameron (1998:121-139). For reaction of the Baltic States in particular see contributions to Jopp and Arnswald (1998).

¹¹⁹ Cited in Avery and Cameron (1998:135).

¹²⁰ The Baltic Review, Winter 1995, vol. 6, "The Baltic states and EU integration", p. 12.

¹²¹ Agence Europe, Brussels, 27.03.1996.

¹²² The Baltic Times, May 30-June 5, 1996, Baltic presidents: we go West together, p. 1.

¹²³ Estonian Review, October 21-27, 1996, President Meri makes state visit to Latvia, p. 3.

¹²⁴ The Baltic Independent, March 3-9, 1995, Estonia skips EU transition period, p.1

EU. The agreement on free trade in agricultural products should be seen in this light. As Estonian Foreign Minister Kallas declared after signing the agreement, "we are going to build our relationship in such a way as to further integrate into the EU"¹²⁵.

Although the agreement on abolishing non-tariff barriers in intra-Baltic trade was signed in November 1997, i.e. after the announcement of the Opinions, its conclusion can also be largely attributed to the "effect of the EU". The agreement illustrates both the potential scope of intra-Baltic economic cooperation and its future limits taking into account individual integration of these countries into the EU. The preamble of the agreement explicitly stated that the final objective of the parties to the agreement is EU membership. Thus, the agreement was instrumental to their integration into the EU. Moreover, EU rules were taken as a reference for the provisions of the agreement thereby illustrating most clearly the role of the EU in solving the coordination problem of choosing the appropriate framework for cooperation. Besides, the costs of economic cooperation measures were minimized as each of the Baltic States was in the process of approximating domestic legislation, including norms governing veterinary and technical product standards, as a part of their integration into the EU internal market.

Coordination problems also explain the failure to advance positive intra-Baltic market integration beyond the scope of integration into the EU, namely the failure to implement the intra-Baltic customs union in 1998. The divergent trade regimes of the three countries, estimated costs related to their alignment, unclear potential benefits as well as the method of sharing the customs duties among the three, proved to be obstacles that policy makers of the three countries have been unable to overcome in the absence of a leader who could supply the rules and side-payments for disadvantaged. The role of the EU in the areas of positive integration extending beyond the scope of integrating candidate countries into the EU is limited. Any proposed economic arrangements among the Baltic States exceeding the scope of their integration into the EU have rather unclear prospects, particularly after one country has started accession negotiations. Differentiation of the Baltic States has further reduced the incentives for intra-Baltic economic cooperation, as policy-makers of these states are provided with new opportunities (or constraints) for achieving their main objectives.

To sum up the analysis presented above and discuss possible future developments of intra-Baltic economic cooperation, the linkages between EU policy and intra-Baltic economic agreements are suggested in the following

¹²⁵ The Baltic Times, July 18-24, 1996, Estonia, Latvia talk security, p. 2.

table. The scheme is based on the categorization of integration stages presented in the theoretical section.

Several remarks need to be made concerning these linkages between EU policy and intra-Baltic economic cooperation. Although it is possible to attribute changes in EU policy to concrete decisions or agreements – signing the Europe Agreements or actual opening of the accession negotiations – the categorization of stages masks the fact that policy changes occur gradually, and cause responses from outsiders sometimes during the preparatory stages. Another feature of this scheme is the emphasis on adaptive policy of the Baltic States based on responses to the developments of EU policy. The EU acts as a policy-maker while Baltic States' governments respond by assessing opportunities and constraints for integration into the Union. In the area of intra-Baltic economic cooperation, policy makers of the Baltic States cooperate when it is likely to increase their chances of membership, which in turn is facilitated by being a part of the same group in respect to the EU.

Table 2. Linkages between EU Policy and intra-Baltic Economic Cooperation

EU policy towards Baltic States	Policy characteristics	Baltic States' integration into the EU	Intra-Baltic economic cooperation
Establishment of diplomatic and economic relations; search for policy options (1991-1995)	Group approach; ad hoc support for sub-regional cooperation	Negative market integration (trade and cooperation agreements; free trade agreements) supported by financial assistance (Phare)	Agreement on free trade in industrial goods
Pre-accession (1995-1998)	Group approach with increasing emphasis on individual developments; strengthened support for sub-regional cooperation	Negative market integration supplemented by unilateral aligning of regulatory policies (Europe agreements, White book), political dialogue and continued financial assistance	Agreement in free trade in agricultural products; agreement on abolishing non-tariff barriers
Accession negotiations (1998-present)	Differentiation; some support for sub-regional cooperation	Positive integration complemented by continued financial assistance; opening of the accession negotiations with Estonia	Failure to implement customs union; possible agreements on free movement of production factors
Membership and transition periods (2007 - ...)	Initial differentiation; formation of issue sub-groups	Positive integration; delegation of authority, participation in decision-making	Possible coalitions inside the EU on certain policy issues (regional policy, etc.)

Source: compiled by the author

Current differentiation of the Baltic States by the EU is likely to reduce possibilities and incentives for increasing the scope of intra-Baltic economic cooperation. The issue is perceived not so much, or not only, of how the development of intra-Baltic economic cooperation can facilitate their integration into the EU. Rather, the question currently is being phrased differently - how differentiation is likely affect the intra-Baltic economic agreements implemented so far. This change of position was rather clearly illustrated by the declaration made by Estonian Foreign minister T. Ilves at the beginning of April, 1998, upon the opening of accession negotiations with the EU. He stated that "we shall seek to ensure that the existing political, cultural and economic relations with our neighboring countries are preserved"¹²⁶. The future status of Estonia's trade regime with the other two Baltic States was to become one of the first negotiation subjects at the beginning of 1999. It is likely that the current market integration measures will be secured, although the prospects for further intra-Baltic economic cooperation are uncertain. Still, the possibility of extending it to include the areas, which are harmonized on the basis of EU rules, remains.

After the official decision to differentiate between the Baltic States in terms of their accession-status and abandon the group approach, the EU continued its support for intra-Baltic economic cooperation, although it seems the emphasis shifted to avoiding negative consequences of differentiation for sub-regional relations. It was reiterated during the meeting of the CBSS in Riga in January 1998 and during the meetings of Association Councils that took place after the Europe agreements came into force in February 1998 which all "welcomed the Free Trade Agreements" that came into force between the Baltic States¹²⁷. In July 1998, Commissioner van den Broek visited Latvia and Lithuania and during his talks with policy-makers of the two countries encouraged them to intensify regional cooperation¹²⁸.

The Baltic States' leaders continued occasionally to declare their solidarity, although the differentiation impacted on the intra-Baltic economic cooperation. Before the Luxembourg Summit, the three presidents agreed on a joint declaration stressing the importance of "full-fledged participation of the Baltic States on equal footing in the European Union enlargement process"¹²⁹. The joint position towards integration into the EU was abandoned after the Luxembourg Summit as were the plans for the intra-Baltic customs union, although the latter issue was brought up in May 1998 by Latvian Minister of

¹²⁶ Agence Europe, Brussels, 01.04.1998.

¹²⁷ DG1 news site, http://www.europa.eu.int/comm/dg1a/daily/02_98/pres_98_48.htm

¹²⁸ DG1 news site, http://www.europa.eu.int/comm/dg1a/daily/02_98/pres_98_671.htm

¹²⁹ The Baltic Times, November 13-19, 1997, Presidential hat trick promises Baltic unity, p.

Agriculture who motivated it by a need to protect the intra-Baltic market¹³⁰. The political tensions resulting from differentiation found expression at the end of April 1998 when the Estonian president was quoted saying in his interview to a Polish newspaper that "Estonia can introduce a visa regime to Lithuanians and Latvians if the European Union requires it"¹³¹. "Baltic unity" was reaffirmed in May 1998 in the joint statement of the three presidents, who also encouraged "the establishment of a more unified economic area, particularly in the fields of transportation, border crossing and the free movement of people, services and capital"¹³². Although the plans for the trilateral agreements on free trade in services and labor were discussed during the routine meetings of the Baltic Council, no decisions have been taken so far and do not seem to be very likely in the near future.

Differentiation has created incentives for new cooperative dynamics among sub-groups formed by members participating in the same stage of integration. The meeting of the five prospective "ins" in Prague before the Luxembourg summit to discuss their integration strategies, and in February 1999 to jointly urge the EU to speed up internal reforms and alter its export policies with regard to CEECs signals new cooperative efforts¹³³. Another sign of a new cooperation dynamics is an increasing number of bilateral meetings between Latvian and Lithuanian authorities in 1998 and 1999. However, it is very unlikely that cooperation inside the new groups of "ins" and "pre-ins" will be extended beyond coordination of their policies towards the EU. Possible changes in group structure reflecting divergent integration rates of individual candidates, limited benefits that could be derived from stronger economic coordination and concentration of resources on accession-related measures all reduce the incentives and opportunities for extending the scope of sub-regional cooperation.

The scope of intra-Baltic economic cooperation also depends on the domestic political economy dynamics in these countries. Difficulties in reaching an agreement on intra-Baltic free trade in agricultural goods and failures to "lock-in" the liberalization of trade that appeared in the end of 1998 and 1999 can be attributed to demands for protection voiced by domestic economic groups. Demands for market integration have been less visible, and so far their impact on intra-Baltic economic cooperation has been negligible. These factors are discussed next.

¹³⁰ Verslo zinios, May 8, 1998, Atgimsta Baltiukso ideja, p. 2.

¹³¹ The Baltic Times, May 7-13, 1998, Meri's EU aspirations irk Lithuania, p. 1.

¹³² The Baltic Times, May 14-20, 1998, Baltic unity remains undivided, p. 8.

¹³³ Lietuvos Rytas daily, February 12, 1999, <http://www.lrytas.lt/19990212/eko12pva.htm>.

VI. INTEREST GROUPS AND INTRA-BALTIC ECONOMIC COOPERATION

A. Demands for Protection

Radical changes in political and economic institutions in the Baltic States have, to a different degree, deprived former economic groups of their influence, while stabilization has gradually produced conditions for emerging new organized groups. This section does not seek to analyze the patterns of organized economic groups' development and activities in the Baltic States. Such task is beyond the scope of this paper, and it is highly complicated by the non-transparent nature of lobbying processes. Rather, it focuses on identifying certain plausible conditions for the divergent demands of economic groups in general and, in particular, those related to intra-Baltic market integration, and its likely future dynamics. First, conditions that seem to have influenced the survival or emergence of new groups are discussed. Then the emergence of demands for protection in as much as they had an impact on intra-Baltic economic cooperation is addressed, followed by a discussion of demands for market integration, or rather the lack of them.

The degree to which the divergent demands of the economic groups have been transmitted to governments and to which governments have been receptive to them has depended on a number of factors, including the structures of national economies, institutional structure of policy-making, ideological commitments and reform strategies. In Latvia and Lithuania, demands for protection as a result of the large agricultural sector, slower privatization involving foreign businesses and more gradual economic reforms, in particular those voiced by agricultural groups or still state-owned enterprises have been stronger than in Estonia. In Latvia and Lithuania, a large share of employment in agricultural sector has made their demands more likely to be satisfied by political leaders concerned about voting effects (see Annex 2). As a result of successive technocratic right wing governments that have been in power in Estonia the demands for protection, which were voiced by agricultural groups, have to a large extent been disregarded. The left wing government formed in Lithuania as a result of "a protest vote" in 1992, has been more responsive to demands for protection from the groups with which old connections were preserved. The right to introduce changes to the trade regime by government decree has further increased the opportunities for demands of economic groups to be satisfied in Lithuania. Gradually, new sectorial organizations for channeling demands have been formed, and, for example, such groups as the Association of Sugar Producers in Lithuania have been rather successful in receiving high protection from competing imported goods. In some cases, organized economic groups have

officially supported certain political parties and have had their representatives in the government, as it has been the case in Latvia and Lithuania.

New political institutions have been established at the beginning of the decade in all three countries. Creating new economic institutions governing market relations has been a more lengthy process. The main market institutions, and the foreign trade regime in particular, were created in 1992-1993. The three countries have tariffed most trade protection instruments, with some quantitative restrictions remaining in Latvia and Lithuania. Although foreign trade regimes have been relatively liberal in each of the three states, particularly in Estonia which from the beginning of reforms was applying zero tariffs to trade, some economic groups have succeeded in preserving tariff barriers or reintroducing them during the course of reforms. For example, in June 1993, the Lithuanian government raised import duties stating that the protection of agricultural workers was one of the objectives of its policy. In contrast, the Estonian government ignored the demands for protection for a long time, even when these were supported by its ministry. As the representatives of the Ministry of Agriculture complained in 1994 if "no measures are introduced then it is likely that Estonian agriculture will not exist in ten years"¹³⁴. Trade policy and responsiveness to demands for protection in Latvia during the period prior to the first measures of intra-Baltic economic cooperation were closer to that of Lithuania. Agricultural interests were particularly strongly represented in the government by the coalition partner, the Farmers Union.

Thus, the intra-Baltic free trade agreement signed in 1993 did not cover trade in agricultural products mainly because the Latvian government was responsive to the demands of agricultural groups, and intended to keep them protected from imports originating in the other two Baltic States. As the representative of the Latvian Ministry of Agriculture declared after the intra-Baltic agreement on free trade in industrial goods came into force, "agriculture is very important for Latvian people, we have to defend our farmers"¹³⁵. Soon after, the Latvian parliament voted to increase the import tariffs further for a number of agricultural products including livestock, pork, beef, lamb, butter, cheese, and eggs, although not without some disagreements with other cabinet members. As in the case of Lithuania, the need to satisfy protectionist demands was based on reference to industrial countries. An "explanation" provided at the time by the representative of the Latvian government was that "these tariffs exist throughout Europe"¹³⁶.

¹³⁴ The Baltic Independent, April 22-28, 1994, Agricultural demands whittled away by EU, p. B2.

¹³⁵ The Baltic Independent, April 8-14, 1994, Baltic free trade deal takes place, p. 1.

¹³⁶ The Baltic Independent, June 17-23, 1994, Farmers push for higher import tariffs, p. B1.

Notably, differences in liberalization schedules agreed on in the bilateral agreements between the EU and each of the Baltic States have been attributed by some to the demands of domestic groups¹³⁷. Conventional import tariffs were raised successively by Latvian and Lithuanian governments, especially on imports of agricultural goods, and on some imported goods that were in competition with similar goods produced locally¹³⁸. In general, import tariffs applied by Latvia and Lithuania have been fluctuating, indicating possible responses to protectionist demands. In Lithuania, for example, import duties were changed over 10 times between 1993 and 1994¹³⁹. In both Latvia and Lithuania, market price support measures and trade barriers to imports of agricultural products increased in 1995-1996, although some barriers were reduced following pressure from the IMF and the WTO (to the latter the Baltic States were seeking to be accepted). In 1997, average import tariffs for agricultural products equaled about 40% in Latvia and about 30% in Lithuania, although conventional import tariffs for industrial goods were much lower¹⁴⁰. High dispersion of import tariff rates with tariffs for some agricultural products, particularly for sugar and dairy products, higher than the average as well as income support measures linked closely to specific products and inputs rather than income groups, indicated likely impact of organized economic groups on economic policy in these countries¹⁴¹. Although with the appreciation of Estonian currency, demands for protection of agriculture gradually moved to the center of political debates in Estonia, the government formed after 1995 elections remained unresponsive to protectionist demands. The possibility of introducing some trade barriers was considered by the Estonian government in 1997 and particularly in 1998 under the pressure of local producers and referring to the future accession to the EU¹⁴².

The differences in political economy dynamics and the resulting foreign trade regimes of each Baltic State were commented upon by the international economic institutions. IMF representatives, for example, were reported in 1995 to characterize Estonia's trade regime as "one of the most liberal trading systems in the world", while Lithuania's trading system was declared to be "almost as open" although its "agricultural sector had been pressing for protectionism"¹⁴³.

¹³⁷ Jurgaitiene and Waever (1996:221). The authors explained the transition period of six years given to Lithuania not only by the reasoning provided by Lithuanian negotiators that transition period was needed to protect Lithuanian agriculture, but also by "the powerful lobby of the formerly privileged industries".

¹³⁸ The Baltic Independent, August 4-10, 1995, New customs duties, p. 5.

¹³⁹ OECD (1996:34).

¹⁴⁰ OECD (1998:19).

¹⁴¹ See OECD (1998).

¹⁴² Verslo zinios, November 4, 1998, Estija keicia kursa, p. 8.

¹⁴³ The Baltic Independent, January 13-19, 1995, Baltics benefit from quick reform, IMF says, p. B3.

At the same time, Latvia's liberalization was described as "less sweeping because the country's powerful agricultural sector has been able to exert considerable pressure for protectionism"¹⁴⁴.

The dynamics of economic interest groups' demands explains the timing of the intra-Baltic free trade agreement in agricultural products. This agreement was foreseen in the free trade agreement signed in 1993. However (and despite EU support), it took several years to agree on it. The agreement to liberalize trade in agricultural products was reached and signed shortly after in May 1996 when the new Latvian Prime Minister Skele fired the Minister of Agriculture who was advocating higher protection for farmers. Skele himself came from the food processing industry, which stood to gain from cheaper imports of raw agricultural products. The agreement was seen as the most beneficial for Estonian producers who could access new markets in the other two states and Lithuanian producers who could increase their sales in Latvian market¹⁴⁵. Latvian farmers were the most concerned about the increase of competition as a result of intra-Baltic liberalization, although the food processing industry was expected to gain. The agreement resulted in 'locking-in' free trade for about one year and a half, until the economic crisis in Russia increased the pressure of adjustment faced by agricultural exporters.

The liberalization of the agricultural and food markets in the Baltic States has increased pressure on the governments to consider abolishing non-tariff barriers which distort competition in the three countries. The demands of economic interest groups also partially contributed to reaching the intra-Baltic agreement on abolishing non-tariff barriers¹⁴⁶. The motivation of domestic farmers and producers was to prevent cheaper imports originating in the third countries. However, soon after the agreement came into force, a number of beggar-thy-neighbor protectionist policies were introduced or threatened to by each of the governments. Most of these measures originated in the protectionist demands of domestic economic groups and resulted in non-cooperative bilateral or trilateral policies.

The economic crisis in Russia, which started in summer 1998, forced producers in the Baltic States to face increasing adjustment pressures. After an initial decline following the reorientation of trade flows to Western Europe, the share of Russia (and CIS) remained significant for the Baltic States, especially for Lithuania where it constituted about 20% of foreign trade turnover (see Annex 2). A large share of exports to Russia from the Baltic States consisted of

¹⁴⁴ Ibid.

¹⁴⁵ The Baltic Review, Summer 1996, Long awaited Baltic Free Trade Agreement Signed, vol. 10, p. 8.

¹⁴⁶ Interview with the official from the Lithuanian Ministry of Foreign Affairs, March 1999.

raw and processed agricultural products as well as locally processed or re-exported industrial goods, the demand for which declined after the start of economic crisis. Some domestic groups responded to adjustment pressures by demands for protection of domestic markets oversupplied by competing products from neighboring countries, while some, not directly impacted by the crisis, tried to take advantage of the situation and use the opportunity for getting protectionist measures to cover imports of competing products. The latter could be said about well-organized sugar producers and producers of fertilizers in Lithuania – the Lithuanian government decided to increase conventional import tariffs for these products among others in October 1998 despite inter-ministerial disagreements¹⁴⁷.

Demands for protection voiced by local producers spilled-over into the area of intra-Baltic economic relations. The possibility of reintroducing trade protection measures in the area of agricultural trade was discussed in a joint meeting of the three ministers of agriculture in September. The Latvian side informed about the possibility of introducing protection measures against exports of meat products and eggs from Estonia and dairy products from Lithuania¹⁴⁸. The need for the intended measures was grounded in the necessity to protect Latvian farmers and producers. Despite the protests of the other partners, at the end of 1998 the Latvian government presented the Parliament with the proposal to introduce quotas for meat exports from Estonia and Lithuania in response to demands from local producers. In the beginning of 1999, the Latvian parliament rejected the proposal to introduce quotas on intra-Baltic trade in selected agricultural goods.

In October and November 1998, Lithuania and Estonia introduced protectionist measures against exports of meat products from each other's market following an exchange of allegations that these products did not conform to veterinary standards. First, the Lithuanian State Veterinary Service accused an Estonian meat company of importing meat from the US and Canada which was unacceptable by EU standards. The Estonian veterinary institution retaliated half a month later by claiming that Lithuanian pork was of unacceptable standards because of injections that were intended to prevent swine disease. The Lithuanian side responded by declaring that Estonian pork contained an objectionable level of lead¹⁴⁹. This time the Estonian side used the EU standard as a reference, which was not seen as safe enough by Lithuanian veterinary service. These disputes took place despite the agreement to respect the decisions of the veterinary institution of one country in the other two. The "pork war" was ended in December.

¹⁴⁷ Lietuvos Rytas daily, October 15, 1998, <http://www.lrytas.lt/19981015/eko15pva.htm>.

¹⁴⁸ Verslo ziniuos, September 25, 1998, "Del latviu ketinimu diskutuos", p. 5.

¹⁴⁹ The Baltic Times, December 3-9, 1998, "Baltics want end to pork war", p. 11, 14.

In the beginning of 1999, intra-Baltic free trade was again distorted by disagreements among Latvia and Lithuania concerning the rules of origin and between Lithuania and the other two countries concerning the threshold prices applied by Lithuania¹⁵⁰. From January 1, 1999, the Latvian authorities refused to recognize product certificates issued in Lithuania for re-exported goods, distorting trade flows between Latvia and Lithuania. Mutual accusations of breaking the rules of the free trade agreement were exchanged, and retaliatory measures were threatened. The Lithuanian Ministry of Foreign Affairs officials accused Latvia of violating the free trade agreement while Latvian Ministry of Economy officials responded by stating that their decisions comply with the new rules of origin initiated by the EU Commission. The disagreement focused on when the new rules were supposed to be enforced. During the meeting in Vilnius in January 1999, Prime ministers of the Baltic States agreed to remove the obstacles to trade. Notably, for the first time demands for anti-dumping policies with regard to bilateral exports were raised by some domestic producers in Latvia and Lithuania. In February 1999, the Latvian government responding to demands of domestic producers started preparing a project to restrict the import of eggs from Lithuania, based on non-compliance to veterinary standards¹⁵¹. On March 17, the Latvian veterinary institution announced the enforcement of restrictions on some exports from Lithuania. In a trilateral meeting several days later the implementation of protectionist measures was denied. In March, the Estonian government accused Lithuania of discriminatory rules of providing subsidies and purchasing pork. Finally, in June, after a strong pressure of Latvian farmers Latvia introduced temporary import tariffs on pork imported from Estonia and Lithuania. The latter threatened to retaliate but import tariffs remained in place.

These protectionist retaliatory policies could be explained by the lack of confidence in partner countries' practices and institutions, lack of information and diverging domestic policies¹⁵². However, taking into account a set of coordinating trilateral institutions and the market situation in the Baltic States, it seems more likely that these measures represented responses to demands of domestic economic groups¹⁵³. The extension of market integration by way of mutual recognition of standards provided opportunities for manipulation of the recognition issue depending on domestic demands. The standards could be manipulated even when they were based on the EU norms. Regulatory

¹⁵⁰ Lietuvos Rytas daily, January 28, 1998, www.lrytas.lt/19990128/eko28ati.htm

¹⁵¹ Lietuvos Rytas daily, February 25, 1999, www.lrytas.lt/19990225/eko251vb.htm

¹⁵² The Baltic Times, December 3-9, 1998, Crisis highlights faults in free trade agreement, p. 11.

¹⁵³ In February 1999, in response to demands of farmers (and against the protests of food producers) Lithuanian government negotiated with the Commission an increase in barriers to raw agricultural imports from the EU.

institutions became a new target of demands for protection, and in some cases non-cooperative measures were prevented only after taking the issue to the top political level. At the same time, budgetary limits for side-payments to the groups facing adjustment pressures made the reintroduction of import protection measures a more feasible instrument of responding to domestic demands. It is likely, that by introducing new standards and norms as part of the EU *acquis* approximation, the increasing regulatory role of state and complexity of regulation will provide more targets for domestic groups' demands and more opportunities for demands to be met. It is also likely that references to the EU Common agricultural policy, despite its uncertain future shape when adopted by the acceding states, are increasingly going to be used as a bargaining tool by domestic interest groups and by governments vis-à-vis other governments.

B. Demands for Market Integration

Business demands for market integration among the Baltic States have been less visible so far. The non-existence of functioning market institutions at the outset of the reforms provides an important explanation for the lack of organized support for liberalization of the market exchange. While demands for protection have often been channeled by often using old connections or open protests and the power of numbers, there has been little organized resistance to protectionist measures or lobbying for the further removal of barriers to exchange. Support from food processing firms in the three countries has been expressed for the conclusion of an intra-Baltic agreement on free trade in agricultural products. It seems like market pressures have also contributed to the abolition of non-tariff barriers to intra-Baltic trade, although their impact on the scope and timing of the agreement is difficult to estimate. Still, in the absence of a strong external motivation, the governments, in Latvia and Lithuania in particular, have been more receptive to demands for protection, which have proved to be stronger and better organized.

The absence of market demands for integration has also been related to an initially low level of business internationalization and the small size of the intra-Baltic market. It should be noted, however, that the level of internationalization of the Baltic economies has been rapidly increasing. International market transactions were liberalized around 1993 and as a result, in the following years the share of foreign trade in GDP of each country reached around 100% illustrating high openness of these economies. In parallel, domestic laws governing foreign direct investment (FDI) have been adopted, although its share until recently has been low in comparison to other CEECs. FDI regimes differ in each of the three states. In Estonia, the relatively liberal regime of FDI and privatization opportunities allowed larger inflows of foreign capital. In Latvia and Lithuania, FDI has significantly increased during recent years, mainly as a

result of a large-scale infrastructure privatization. In 1998, the net FDI was expected to reach 200 million USD in Estonia, 344 million USD in Latvia and 800 million USD in Lithuania¹⁵⁴. These facts, however, reveal little without considering the size and nature of economic relations between the Baltic States.

The combined size of the Baltic States market is around 8 million people. Although the GDP per capita has increased significantly during the decade, it is still significantly below the level of the EU average (see Annex 2). The share of the intra-Baltic market could be well illustrated by a comment of a Western businessman was reported to have noted that the combined incomes of Estonians, Latvians and Lithuanians did not reach the incomes of workers in the Empire State Building in New York¹⁵⁵. The limited potential for intra-Baltic trade growth has been also indicated by the gravity models according to which intra-Baltic trade flows exceeded their potential¹⁵⁶. Potential for trade growth with EU countries was estimated to be significantly higher than for intra-Baltic trade. Intra-Baltic trade flows have been increasing in both absolute and relative terms, although mainly reflecting general trends of growth (see Annex 2). Furthermore, a low level of intra-industry trade has limited the opportunities for economies of scale. It has been noted that such labor-, skill- and resource-intensive industries as clothing, footwear or textiles favor small and flexible units of production, so possibilities for economies of scale in the region seemed to be limited¹⁵⁷. The gains from economies of scale are restricted by the relatively large share of trade in agricultural goods. Similarities in production structures are likely to constrain potential for complementarities in trade¹⁵⁸. However, increasing imports of updated technology and growing FDI might create new opportunities for gains and alter specialization patterns in the long run.

Thus, the gains from active lobbying for intra-Baltic market integration have so far seemed to be low, especially taking into account transition-related problems which businesses had to deal with in each of the countries. The issue of customs administration has been an exception frequently provoking strong criticisms of businesses in the three countries. The problems related to the functioning of the customs systems were acknowledged by the governments, although their upgrading was undertaken mainly with the technical and financial

¹⁵⁴ EBRD (1998:214-221).

¹⁵⁵ The Baltic Times, December 3-9, 1998, Foreign investment key to Baltic success, p. 13. Although the relevance of such a comparison is doubtful, it well illustrates the attitude of large foreign investors towards opportunities provided by intra-Baltic market.

¹⁵⁶ Hernesniemi (1996:6-8). Its should be noted that intra-Baltic trade potential could have been underestimated due to a large share of shadow economy and rapid growth of incomes.

¹⁵⁷ Pautola (1996:15).

¹⁵⁸ Sorsa (1997:16).

assistance of the EU. The EU also played a role in encouraging the setting up of intra-Baltic business organizations, which could press for removal of obstacles to market exchanges. Proposals for setting up intra-Baltic business organizations such as a Baltic Chamber were voiced during the meetings organized by the EU, the OECD or the CBSS which also provided opportunities for the exchange of information among business and governments of the sub-region¹⁵⁹. However, for a number of reasons, including the absence of a single institutional target for demands and relatively small gains from organized lobbying efforts, joint business actions have not been visible.

Although possible gains from intra-Baltic market integration are limited, market strategies employed by foreign investors and domestic companies have contributed to the informal integration of the three economies. There has been an increasing tendency for some multinational corporations to establish operations in one of the three Baltic States as a base from which they serve all the Baltic market. For instance, Coca-Cola has its bottling factory in Estonia, Kellogg has headquarters in Latvia and McDonald's Restaurants have headquarters in Lithuania. Examples in the service sector are the establishment of the French bank Societe Generale in Riga, and opening of an office of German Norddeutsche Landesbank in Vilnius. As was observed, these are just a few examples of what is a much wider phenomenon of international companies that establish themselves in one of the three states and serve the regional market¹⁶⁰. They illustrate how international companies treat the intra-Baltic sub-region, and the degree, to which international investment in this region might be tied to intra-regional trade and supplement it. Still, it should be noted that the dominant motivation of foreign investors to locate in the Baltic States is related to opportunities offered by the Eastern markets which can be served from the Baltic countries.

Another recent phenomenon illustrating the emergence of a regional approach towards the Baltic States in business is the growth of intra-regional investment. For example, in October 1998, Estonian investments in Lithuania equaled about 40 million USD, while Latvian investments in Lithuania made up about 9 million USD¹⁶¹. One of the first examples was the Estonian Hansa Bank that expanded its activities in financial services in the other two Baltic States. As some observers have noted, Estonian enterprises have started turning into

¹⁵⁹ The first round-table was organized by the EU in May 1994 in Riga and brought together EU industrial representatives, members of the Commission, Baltic States governmental officials and business. Its purpose was "to unite industrialists and public authorities of all three Baltic republics", as the Commissioner Mr. Bangemann said. (<http://www.europa.eu.int/rapid>, DN:IP/94/406).

¹⁶⁰ Lesser, Muravskaya, Shumilo (1997:20).

¹⁶¹ Interview with official from the Lithuanian Ministry of Foreign Affairs, March 1999.

"Baltic trans-nationals" at a fast rate by relying on subcontracting and the establishment or purchase of a company in the other Baltic States¹⁶². A similar trend was demonstrated by other business activities. The Vilnius Bank from Lithuania, after buying the Latvian financial firm Latvijas KIF Grupa, has started activities in the Latvian securities market. The strategic cooperation agreement signed by the three major Baltic banks - Estonian Uhispank, Latvian Unibanka and Lithuanian Vilnius bank - in March, 1998, seem to provide an example of the possible creation of a joint cross-border banking unit that would be operating in all three Baltic states in providing cross-border customer service, joint investment and development projects, and inter-bank services. It should be noted that inflows of FDI into the Baltic States, from Scandinavian countries in particular, have contributed to emergence of Baltic alliances link by the ties of ownership. There is also a tendency towards closer cooperation and participation in the insurance, leasing and brokerage services. For example, the representatives of the three stock exchanges have been discussing the idea of a joint Baltic stock exchange, although the Lithuanian side has been reluctant to advance this project, suggesting that gains from the intra-Baltic stock exchange would not exceed significantly the costs of its establishment¹⁶³.

These processes could lead to increased business concentration due to increased competition and might create pressure for the harmonization of the business environments in the three countries leading to spill-over effects in promoting the creation of the intra-Baltic common market. Coordinated policies in such areas as transport might be further developed in order to exploit the transit position of the sub-region and facilitate large flows of transit trade. However, the potential impact of informal integration in generating demands for common intra-Baltic policies and positive integration is likely to be limited. It is more likely that policies governing market relations will be aligned by autonomously harmonizing them with EU *acquis*, and not by intra-Baltic economic cooperation.

VII. CONCLUSIONS

This paper has argued that the scope and timing of intra-Baltic economic cooperation can be explained by "the EU effect" and demands of economic interest groups. The analysis provided seems to support the argument. First, the role of the EU as a supplier of rules and supporter of sub-regional cooperation as an informal precondition for integration into the EU has been crucial in advancing intra-Baltic market integration schemes. However, integration into the EU has been given higher priority by Baltic States' policy-makers than intra-

¹⁶² The Baltic Review, Spring/Summer 1997, Moving towards a common economic space, p. 10.

¹⁶³ Verslo zinios, October 28, 1998, Baltijos saliu birzos nori jungtis, p. 3.

Baltic cooperation. Therefore their willingness to pursue sub-regional economic cooperation has depended on its instrumental utility in advancing integration of their countries into the EU. The instrumental value of intra-Baltic economic cooperation was higher when the three countries were at the same stage of integration into the EU, while it has decreased after the policy of differentiation of the applicant states was adopted by the EU.

It seems unlikely that intra-Baltic economic cooperation will extend to other areas of market integration. It is very likely that during the European Summit in Helsinki at the end of 1999, both Latvia and Lithuania will be invited to start accession negotiations with the EU. This will again raise the issue of differentiation. However, it seems that the divergent dynamics of membership negotiations can act as the main constraint on further intra-Baltic cooperation (especially if Latvia and Lithuania are invited to start the actual negotiations at different points in time). It is still unclear what effects the possible accession of one country is likely to have on sub-regional economic cooperation. The impact to a large extent will also be determined by the outcome of membership negotiations. The economic and political impact of enlargement in stages on sub-regional economic cooperation is difficult to estimate. Possible trade and investment diversion resulting from differentiation might reduce the market pressure for sub-regional integration and strengthen demands for protection. However, the negative economic effects are likely to be insignificant, taking into account the continuing integration of the three into the EU. The other issue is to what extent the sub-regional approach can be maintained when the Baltic States become EU members. The dynamics of intra-Baltic relations does not seem to provide evidence for the bargaining power argument. The bargaining positions in the Council might be coordinated depending on the policy area. However, the willingness to coordinate positions on economic policy issues is going to a large extent to be determined by domestic political economy forces.

The demands of domestic economic interest groups have exerted considerable influence on the dynamics of intra-Baltic economic cooperation. The demands for protection, voiced by agricultural groups in particular, account for stops in intra-Baltic market integration and recent retaliatory policies. The governments in Lithuania and Latvia have been more receptive to demands for protection than to complaints voiced by the groups facing losses from the protectionist policies. The demands for market integration have been much less visible due to institutional changes and transition-related domestic problems in the three countries as well as limited potential gains from intra-Baltic market integration. The informal integration of the three economies has shown some signs of generating pressure for extending the scope of economic cooperation. However, its impact on policy making is unlikely to be significant, and the

aligning of regulations will tend to take place on the basis of the unilateral adoption of the EU *acquis* rather than result from intra-Baltic cooperation.

The recent instances of protectionism and non-cooperative policies provide some grounds for future projections. Faced with adjustment pressures, disadvantaged economic groups are likely to strengthen their demands for protection. The governments constrained by budgetary limits are likely to be more responsive to their demands. The extension of market regulation and its increasing complexity provides more opportunities for protectionist measures to be introduced. The rules of the EU might be used as a bargaining tool by economic groups, especially as the integration into the EU of each of the state progresses. The progress of agricultural policy and budgetary reforms in the EU might further set an example that could be referred to by domestic groups in the Baltic States and by the governments *vis-à-vis* each other.

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Annex 1

Table 1. The Main Bilateral Economic Agreements between the Baltic States and the European Union

Agreement	Signed	In force	Main provisions
Trade and Cooperation Agreements	11.05.92	01.02.93 (for Latvia, Lithuania) 01.03.93 (for Estonia)	Most favorite nation status, non-discrimination; extension of EU generalized system of preferences; economic cooperation in some areas
Agreements on Trade and Trade related matters	18.07.94	01.01.95	Liberalization of trade based on GATT principles; free trade in industrial goods (CN 25-97); 4 years transition period of gradual liberalization given to Latvia, 6 years transition period of gradual liberalization given to Lithuania; standard protection clauses; Joint committees to oversee the implementation of the agreements
Association (Europe) Agreements	12.06.95	01.02.98	Objectives of Estonia, Latvia and Lithuania to become EU members acknowledged; the provisions of free trade agreement incorporated; political dialogue; economic cooperation in areas such as competition policy (EU rules), movement of services, capital and labor, establishment, protection of intellectual property rights, consumer protection, approximation of laws, cooperation in other areas such as industrial policy, science and technology, energy, environment, etc.; Association Council to supervise the implementation of the agreement and Association Committee

Source: respective bilateral agreements

Table 2. Instruments of Baltic States' Integration into the European Union

Instrument	Main features
Pre-accession strategy	
(1) Europe agreements	See table 1.
(2) Phare program	Technical assistance for transition and pre-accession measures in applicant countries.
(3) White paper on preparation of the associated CEECs for integration into the Internal Market of the Union	Identifies key measures in each sector of the Internal Market and suggests a sequence in which the approximation of legislation with EU <i>acquis</i> should be undertaken.
Accession partnerships	Define country specific need in order to support the applicant country in its preparation for the membership. Measures are based on the needs identified in the Opinions and aim to meet accession (Copenhagen) criteria. Provide financial assistance needed for further implementation of priority measures.
National Programs for the Adoption of the <i>Acquis</i>	Define actions needed to reach objectives set out in the Accession partnership. Structurally are based on the Opinions and Progress Reports.
Screening	Analytical examination of the <i>acquis</i> .
Twinning	Aims at reinforcing institutional and administrative capacity. Consists of technical assistance, training programs, exchange of experts, participation of applicant countries' officials in the EU programs.
Accession negotiations	Aim at agreement between the EU and a candidate country on terms of accession. Currently are taking place between the EU and Estonia.

Annex 2

Table 1. Gross Domestic Product by Economic Activity in 1998, %

	Estonia	Latvia	Lithuania
Agriculture, hunting and forestry	4.6	4.5	11.7
Fishing	0.4	0.2	0.0
Mining and quarrying	1.4	0.2	0.5
Manufacturing	14.2	20.2	20.5
Electricity, gas and water supply	5.5	3.9	4.2
Construction	4.7	5.2	7.7
Trade	15.6	17.5	16.5
Hotels and restaurants	1.1	1.0	1.8
Transportation, storage and communications	14.2	14.2	9.6
Financial mediation	4.7	3.2	2.4
Real estate, renting and other commercial activities	12.6	5.9	7.2
State governance, national defence and mandatory social security	4.7	10.0	5.9
Education	5.6	6.6	5.5
Health and social care	4.0	3.4	3.6
Other communal, social and personal services	6.7	4.0	3.0

Source: Statistical Office of Estonia, Latvian Statistical Office, Lithuanian Department of Statistics

Table 2. Employed persons by economic activity, 1998, May, %

	Estonia*	Latvia	Lithuania
Agriculture, hunting and forestry and fishing	9.5	18.7	19.3
Manufacturing, mining and quarrying	23.0	19.2	19.5
Electricity, gas and water supply	2.7	2.4	3.1
Construction	7.5	5.6	6.9
Trade and different repair works	14.0	14.6	14.7
Transport and communications	9.3	7.9	6.7
Other services	34.1	31.7	29.8

* 1998, 2nd quarter

Source: Source: Statistical Office of Estonia, Latvian Statistical Office, Lithuanian Department of Statistics

Table 3. Selected Macroeconomic Indicators, 1998

	Estonia	Latvia	Lithuania
GDP per capita in current prices, US \$,	3591	2611	2887
GDP per capita in PPS expressed as % of the EU15 average	37	27	30
Foreign debt as a share of projected GDP, %	4.2	6.1	15.7
State budget deficit as % of GDP	0.3	0.2	1.2
State debt as % of GDP	55.0	9.9	22.4
Export of goods and services as % of GDP	61.9	27.8	34.7
Direct foreign investment, mil. US \$ (cumulative)	1811	1488	1625
EU share in direct foreign investment, %	75.5	40.1	60
Current account deficit, %	8.6	11.1	12.1

Source: Statistical Office of Estonia, Latvian Statistical Office, Lithuanian Department of Statistics

Table 4. Export Structure by Trade Partners in 1998, %

	Estonia	Latvia	Lithuania
ES	54.8	56.6	37.4
CIS	20.9	19.0	36.2
Baltic countries	12.4	11.9	13.9
Other	11.6	12.5	12.5

Source: Statistical Office of Estonia, Latvian Statistical Office, Lithuanian Department of Statistics

Table 5. Import Structure by Trade Partners in 1998, %

	Estonia	Latvia	Lithuania
ES	60.1	55.3	47.3
CIS	14.2	16.0	26.0
Baltic countries	6.1	12.9	3.3
Other	19.6	11.5	23.4

Source: Statistical Office of Estonia, Latvian Statistical Office, Lithuanian Department of Statistics

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