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Introduction

Prior to the disintegration in the late 1980s of the Soviet bloc and then the Soviet Union itself, most of the economies in eastern Europe were members of CMEA/COMECON (the Council of Mutual Economic Assistance) that was formed to divert trade away from the market economies in the west.¹ The development, under Soviet planning, of strong input-output linkages between industries in different countries/republics led to a significant degree of complementarity between member economies. This complementarity successfully diverted trade away from non-members, facilitating the maintenance of high degrees of in-bloc self-sufficiency. The feasibility of barter trade between members also contributed to this process by helping these countries overcome their hard currency constraints (Gultekin and Mumcu, 1996). Following the collapse of the Soviet bloc and hence of CMEA, the ex-Soviet republics gained independence while the formerly socialist nations of eastern Europe became exposed to competition for global markets amongst the market economies. A considerable portion of trade in these markets was controlled by regional trade blocs. So, when Turkey – then perceived to be a regional power with a relatively well-functioning market economy – called for the formation of a regional economic co-operation zone between the countries around the Black Sea in 1990, Armenia, Azerbaijan, Bulgaria, Georgia, Moldova, Romania and Russia immediately responded by sending representatives to Ankara, Turkey to discuss the project.

Turkey's call for the Ankara meeting was motivated by the country's evident interest in restoring the regional peace and stability that had been disturbed by the profound changes of the late 1980s in the neighbouring areas. The Turkish government viewed the development of vested interests through economic co-operation as the best way to maintain peace. This would put an end to animosities and ethnic grievances in the Balkans and the Caucasus, leading to welfare gains for all the parties involved (Sayan and Zaim, 1998). Thus, when the formation of a regional organisation for economic co-operation between the countries on the Black Sea had first been suggested in 1990 by Ambassador Sukru Elekdag, former head of the Turkish mission in Washington, DC (Togan, 1994),² the Turkish government quickly responded by starting a campaign to promote the idea (Garih, 1995). This led to the organisation of the Ankara meeting.

At the end of the Ankara meeting, the representatives declared officially that they had agreed to form a Black Sea Economic Co-operation (BSEC) zone together with Turkey. Other transition economies in the region also viewed Turkey as a likely source of financial and technical assistance, and the group was soon joined first by Ukraine and then Albania.

- 1 The only exceptions were (former) Yugoslavia and Albania (which joined in 1949 but withdrew in 1962).
- 2 For a list of articles on BSEC written by Ambassador Elekdag himself, see Kut (1995).

Greece also applied to join and was granted membership. With the signing of the BSEC Summit Declaration in June 1992 in Istanbul,³ BSEC was born as one of the first regional organisations aiming to develop economic co-operation between the members of the two adversary alliances of the Cold War era: NATO and the Warsaw Pact.⁴

At the time of the formation of BSEC, only the NATO-affiliated members, Greece and Turkey, had market economies, whereas the other nine were still centrally planned economies with practically no private sector involvement in economic activities. Due both to this special composition of its members and the specific nature of their experience, BSEC emerged as, and has largely remained, an exceptional regional arrangement (Sayan and Zaim, 1998). It has worked since 1992 to facilitate the growth of natural (as opposed to diverted) trade between its members, as well as to contribute to the overall development process of its members through a somewhat loose form of regional co-operation. For example, instead of requiring its members to reduce or eliminate right from the beginning any conventional (tariff or non-tariff) barriers within the co-operation zone, BSEC aimed to help relax the *structural* constraints preventing larger volumes of trade between members by contributing to the transition process through which its ex-socialist members were passing. Even now, as it prepares for its Decennial Summit on June 25 2002, BSEC continues to stop short of requiring strong commitments from its members and maintains its permissive approach to regional economic co-operation.

The purpose of this article is to evaluate the experience of BSEC and to seek an answer to the question of whether regional economic co-operation in this broader sense could lead to any significant benefits for members, even when the co-operating partners are not required either to take such concrete steps as liberalising trade between themselves and/or to harmonise their policies towards third parties. The next section describes the nature of co-operation within BSEC while section three concludes with a general discussion.

Nature of co-operation through BSEC

In conventional trade theory, the fundamental motivation behind the regional arrangements is to improve the welfare of members through the reduction or elimination of barriers to trade within the region. The members of the regional arrangement would enjoy welfare gains as long as the welfare-improving *trade creation* (TC) effects exceed the welfare-reducing *trade diversion* (TD) effects. TC arises when domestic production in a certain sector of a member country is replaced, in part or as a whole, by imports from another member which has a *comparative advantage* in the production of that sector's output. Since the member with a comparative advantage is, by definition, a country

3 The full text of the BSEC Summit Declaration can be found in BSEC (1995): *Handbook of Documents* (Vol. I), Istanbul: BSEC Permanent International Secretariat, pp. 3-6. An online version of this document is at <http://www.mfa.gov.tr/BSEC/SummitDeclarationBsec.htm>.

4 The Council of Baltic Sea States (CBS), formed a few months before BSEC, is another similar organisation. For information on the membership composition and the goals of CBS, see OECD (1997): *Designing New Trade Policies in the Transition Economies*, Paris: OECD.

which produces that output at a lower cost, i.e., more efficiently, there are welfare gains associated with trade creation. TD, on the other hand, occurs when the elimination of barriers upon imports from partners lowers the cost of those imports below the cost of imports from more efficient third parties, as the latter remains artificially high due to the maintenance of restrictions on third party imports. Naturally, such a switch from more to less efficient producers would decrease the importing member's welfare.

This is the standard framework for analysing the potential welfare effects of the regional arrangements formed to facilitate trade between market economies, but applying it to the case of BSEC requires special attention to be paid to the peculiar characteristics of the member economies and the nature of the co-operation within BSEC itself. This warning applies since, unlike other forms of regional arrangements between market economies, the BSEC agreement does not directly provide for any trade preferences for countries within the group (OECD, 1997). BSEC has not required strong commitments towards the harmonisation of commercial policies *vis-à-vis* third parties, or reductions in tariff or non-tariff measures for trade between members, so co-operation through BSEC would not have been expected to change the relative costs in domestic markets of imports from member and non-member countries. For this reason, neither trade diversion nor trade creation effects in the sense described above were likely to arise due solely to BSEC membership. However, BSEC has contributed to a lowering of the barriers to trade between the member countries. But, unlike those analysed in the existing integration literature, the barriers in this context were not of the type that nations artificially erect by introducing tariff and non-tariff measures of protection and which, once decided, could be removed instantaneously. Instead, the barriers to trade between BSEC members were the structural barriers that had been formed over long periods of time most of which, even in the presence of political will, could not be eliminated as quickly as conventional barriers. So, BSEC could only help create trade in a slightly different sense than the one suggested by the conventional definition of TC (Sayan, 1998a and b; Sayan and Zaim, 1998).

In fact, it was the recognition of the special structural conditions of the members that shaped the co-operation arrangement which BSEC was expected to create. It was recognised during the multilateral talks preceding the establishment of BSEC that full economic integration would not be an *a priori* commitment for the participants, even though consideration towards such integration could be given later in the process of co-operation.⁵ Co-operation would be developed gradually, by taking into account:

The specific economic conditions, interests and concerns of the countries involved, and particularly the problems of the countries in transition to the market economy (Article 10).

The priorities for different areas of co-operation would be determined during the process itself, with:

- 5 In fact, a 'Declaration of Intent for the Establishment of a BSEC Free Trade Area' was signed in February 1997 as a further step in co-operation. The actual formation of such a free trade area, however, is not likely in the near future (for the text of the 'Declaration of Intent', see PABSEC (1997): *PABSEC* (the Magazine of the Parliamentary Assembly of BSEC), Vol. 7 (June)).

The achievement of a higher degree of integration of the Participating States into the world economy, (Article 5)

set as a major goal. Within this framework, the participating states agreed to promote co-operation by contributing, among others:

... to the expansion of their mutual trade in goods and services and ensuring conditions favourable to such development by continuing their efforts to further reduce or progressively eliminate *obstacles* of all kinds, in a manner not contravening their obligations towards third parties [Article 14; emphasis added.] (BSEC, 1995: 5)

Given the special composition of BSEC membership, the reference in this Article to the reduction/elimination of 'obstacles' must not be viewed as a call for a removal of conventional barriers to trade. It must be viewed, instead, as a call for co-operation towards a relaxation of the structural constraints that have played a more important role in preventing greater volumes of pre-BSEC trade between members – especially between the transition economies joining BSEC, on the one hand, and Greece and Turkey, on the other. In fact, at the time of the formation of BSEC, Greece was a full member of the EU and Turkey was negotiating a customs union with it. So, there was actually little leeway for BSEC to set the levels of conventional barriers independently and without contravening commitments with third parties. Hence, BSEC could have a potentially significant effect on trade flows in its area only through its contribution to the removal of the structural 'obstacles' that had prevented greater volumes of trade between Greece and other members. In other words, the potential of BSEC to generate any trade creation effects, or to reverse the diversion of trade between the ex-CMEA partners joining BSEC, would depend on its ability to tackle the structural obstacles that existed prior to its formation.

Some of these structural obstacles were to do with the lack, or the inefficiency, of channels for trade and which act to suppress all bilateral trade flows between members (with the possible exception of trade between Greece and Turkey).⁶ The others cover the ideological differences that once existed between members that belonged to the different alliances of the Cold War era, and the associated differences in their trade regimes. Coupled with the artificially created complementarity, or interdependence, between the economies of the ex-socialist members, these structural factors had effectively created two different patterns of pre-BSEC trade between current members:

1. the sizeable, but largely diverted, trade between the former Soviet bloc countries
2. the relatively insignificant volumes of trade that these countries had with Greece and Turkey, despite the geographic proximity between the two groups.

Given the initial lack of private capital accumulation, and the absence of private trading companies and commercial banks (Maurel and Cheikbossian, 1998), there were no barriers that could be easily removed by BSEC for the purposes of welfare gains

6 As noted in Maurel and Cheikbossian (1998), the transportation costs in the eastern European area were higher than the average for the rest of the world. The high transportation costs can be attributed to the inefficiency of channels for regional trade.

through increased trade. In fact, part of the pre-BSEC trade that happened to take place between pairs of current members (e.g. between Turkey and Romania, or between Greece and Bulgaria) was trade between NATO and Warsaw Pact members that was carried out despite the serious difficulties posed by regulations which restricted trade in some sectors across the blocs, differences in property rights and trade regimes (forcing Greek and Turkish exporters to deal only with inefficiently operating state trading companies and banks) and the hard currency constraints faced by the then-centrally planned members.⁷ Likewise, the lack of common product standards prevented trade in many sectors, limiting it mostly to raw materials and primary commodities.

As for the role of the structural factors that result from the lack, or the simple inefficiency, of trade channels, the meagre state of the transportation and communications infrastructure that is still common to many ex-socialist members needs to be considered. In these circumstances, increasing the volume of trade would, again, take more than the reduction/elimination of tariff and non-tariff barriers through a trade liberalisation agreement. Even in the complete absence of such conventional measures of protection, the poor infrastructure for transportation and a lack of dependable communications facilities would have imposed structural barriers, physically preventing greater volumes of bilateral trade between any pair of members, including those Warsaw Pact/CMEA members (Sayan, 1998a and b).

Some of these structural barriers, such as the ideological differences, had been removed before the establishment of BSEC,⁸ but others nevertheless remained. The peculiarity of the nature of the structural obstacles assigned BSEC special roles that no regional organisation had assumed before. The absence of a private sector and the associated lack of private capital accumulation amongst the ex-socialist members posed exceptional difficulties. As this could act as a major hindrance to economic co-operation, the organisation assumed the task of helping the structural transformation of these members by contributing to the creation of a market economy led by the private sector: Article 13 of the Declaration required co-operation in all fields to be achieved via the identification, development and implementation of projects of common interest through the active participation of private enterprises and firms, reflecting the organisation's commitment to the market economy.

Fields for potential co-operation were identified through a rather extensive list. The establishment of the BSEC economic area was meant to serve first the promotion of economic co-operation (especially trade and industrial co-operation), but it was also intended to cover science and technology and the environment, as well as the following areas where concrete steps towards co-operation were required: transport and communications, including their infrastructure; informatics; exchange of economic and commercial information,

7 Even shortly after the emergence of BSEC, the lack of banking regulations for the financing of international trade in some of the ex-socialist members of BSEC proved to be a major obstacle which led many Turkish exporters to ignore orders from these countries (Sayan and Zaim, 1998).

8 As a matter of fact, BSEC could not have been formed had these ideological differences remained.

including statistics; the standardisation and certification of products; energy; the mining and processing of raw minerals; tourism; agriculture and agro-industries; veterinary and sanitary protection; and health care and pharmaceuticals (Article 13).

The steps that BSEC has so far taken to help overcome the structural obstacles can best be described in reference to its organisational structure. In order to secure the active participation of the private sector in accomplishing projects of mutual interest, the BSEC Council, later renamed the BSEC Business Council (BSECBC), was founded in 1992. The purpose of BSECBC⁹ is to provide open channels for regular interaction between the national business communities of the members and governmental bodies involved in BSEC. For this purpose, the BSECBC develops and maintains a network of useful contacts through bilateral business councils and chambers of commerce, and similar national organisations. The Council, operating through the Permanent Secretariat based in Istanbul, is currently active in identifying both private and public investment projects that are of common interest to members.⁹

The BSECBC acts as the business component within a larger organisational structure which also includes governmental, parliamentary and financial components, and a permanent international secretariat working under the supervision of the BSEC Sessional Chair. The Parliamentary Assembly (PABSEC), the parliamentary component of BSEC, was created in 1993 by the representatives of member countries other than Bulgaria and Greece. The governmental component consists of the decision-making body, i.e., the Meeting of the Ministers of Foreign Affairs (MMFA), the Sessional Officials Meeting and the Expert Working Groups (WGs). These working groups are subsidiary bodies established by the MMFA to deal with concrete issues of co-operation in the areas listed above. Some of the groups established so far include: agriculture and agro-industry; banking and finance; energy; environmental protection; exchange of statistical data and economic information; promotion of technology transfer; co-operation in science and technology; co-operation in tourism; and avoidance of double taxation. These working groups have been instrumental in the completion of several projects designed to develop co-operation in the respective fields, including the establishment of the BSEC Co-ordination Centre for the Exchange of Statistical Data and Economic Information and the Black Sea Trade and Development Bank (BSEC, 1995). Headquartered in Thessaloniki, Greece, the Bank began operations in 1999 as the first of its kind in the region. Jointly financed by the eleven member states, the Bank represents the financial component of the BSEC structure and, with an initial capital adding up to \$300m (to be increased to \$1.5bn), is in the process of becoming the principal source of financing for the implementation of joint regional projects.

Joint regional projects mostly focus on areas which will help relax the structural constraints affecting the efficiency of channels for trade. Considering the importance of the issue, a working group on transport and communications was set up very early on in the beginning of the co-operation through BSEC. Later in December 1993, this working group was divided into two – one on transport and the other on communications. Some of the projects recommended by the groups have already been completed, including the estab-

⁹ Visit <http://www.bsec-organization.org/council.htm> for detailed online information about BSECBC activities.

ishment of fibre optic communications networks and radio link systems to connect Turkey to: i) Bulgaria, Romania and Moldova (KAFOS); ii) Italy, Ukraine and Russia (ITUR); and iii) Azerbaijan and Georgia (DOKAP) (Sayan and Zaim, 1998). Work on other projects aiming to integrate highways, railways and maritime lines so as to improve the efficiency of transportation networks between members is currently under way.

To summarise, BSEC has so far used its limited financial resources to help its members in the process of both socio-economic transformation and the improvement of infrastructure by initiating co-operation in a number of fields, some of which would probably not be typical priority areas for other regional organisations formed by market economies.¹⁰ Other fields of co-operation that are more directly related to the trade potential of members include the standardisation of products to be traded and the harmonisation of customs regulations. BSEC has also had to form an *ad hoc* working group on the travel of business representatives) to assure the speeding up of customs formalities and the easing of national visa regulations, etc., so as to facilitate travel within the BSEC area by business people from the member countries. Despite its use of such unconventional means, it can be argued, based on the limited empirical evidence available in the literature (Sayan, 1998a and b), that BSEC has managed to contribute to trade creation in the region thereby mimicking the conventional role played by other regional initiatives.

Concluding remarks

The Black Sea Economic Co-operation (BSEC) zone, formed in 1992, was one of the first formal initiatives that aimed to develop economic co-operation between countries that were once members of the two adversary alliances of the Cold War era. Greece and Turkey, the NATO-affiliated members of BSEC, became partners with their formerly communist neighbours: Albania; Armenia; Azerbaijan; Bulgaria; Georgia; Moldova; Romania; the Russian Federation; and Ukraine. The partnership required co-operation in quite a comprehensive list of areas, including trade, but without providing a basis for any preferential treatment for trade between members.

After completing the initial formation stage (the period between the BSEC Summit Declaration of June 25 1992 and the establishment of the BSEC Permanent International Secretariat on March 10 1994), BSEC entered into the so-called consolidation stage, marked by the Bucureşti statement of the high-level meeting of the heads of state or government (June 30 1995) and the Moscow Declaration of the heads of state or government (October 25 1996). Then, on June 5 1998, the Yalta Summit of the heads of state or government convened and signed the BSEC Charter. Following ratification by the parliaments of the member states, the Charter came into force, marking the official inauguration of the Organisation of the Black Sea Economic Co-operation on May 1 1999. With the enduring commitment of the eleven signatories as pledged by this Charter, BSEC acquired a new status as a regional economic organisation with its own legal identity. The legally-binding Charter replaced the political İstanbul Declaration as its

10 Such as establishing a parliamentary assembly like PABSEC to work at strengthening pluralist democratic structure and political stability in the BSEC area.

principal code. Finally, with the İstanbul Summit Declaration of the heads of state or government on November 17 1999, BSEC effectively moved into the stage of instituting its own programmes and projects.

The BSEC area represents a geographically diversified territory of nearly 20 million square kilometres that is currently populated by 330 million people. It is second only to the Persian Gulf area in terms of its oil and natural gas reserves and it has rich deposits of various minerals and metals. This rich natural resource base is coupled with human resource endowments made up of an often competitive and well-educated labour force. Albeit that some of it needs serious restructuring and modernisation, the area also has a significant manufacturing capacity.

In terms of the purchasing power parity values of their per capita GDPs, Albania is the poorest member and Greece the richest. With the exception of Albania and, possibly, of Georgia, all the members can be considered middle or upper-middle income economies. It must be noted, however, that some members have experienced wild fluctuations in their GDPs after the commencement of their transition to a market economy.

BSEC has emerged as a regional initiative encouraging co-operation and improved market access rather than protection and preferential treatment. It has helped its members improve their ability to link with the global economy and has created welfare gains through increased trade between its members. Even though it did not emerge as a strong form of regional integration *per se*, the BSEC Summit Declaration reflected an early awareness of the potential role that regional co-operation could play in this area and assigned a high priority towards assistance to transition members struggling to connect with the world economy.

With all these characteristics of its members, and its almost unique nature, BSEC certainly deserves more attention than it has actually received in the literature. BSEC experience must be studied further, and extensively, as the organisation could act as a role model for other regional initiatives.

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