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The Latvian Institute of International Affairs launches its first annual Foreign Policy Yearbook to address the issue of continuity and change in Latvia's foreign policy. Although this analytic endeavour brings together authors with a diversity of backgrounds, we are united in our willingness to facilitate the understanding of the place and tools of a small country in international affairs. This publication reflects on the major foreign policy vectors, outlines views on prospective developments, introduces additional themes and provides policy recommendations.

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INTRODUCTORY REMARKS

Andris Sprūds

The world has experienced transformative developments in recent years. The architecture of the international political and economic order has undergone a gradual reconfiguration. The economic recession, European dilemmas, the shale gas revolution, turmoil in the Middle East, China's continuous rise and Russia's regional ambitions are among a number of game changers, opportunities and challenges to the global system and its leadership. On the positive side, the concerns of approaching economic disaster with considerable social and political repercussions have been alleviated and gradual growth has re-appeared. At the same time, domestic instabilities and geopolitical competitions create global and regional tensions.

Latvia has essentially continued deepening its Euro-Atlantic integration in 2013. The country received the "green light" to join the eurozone and to start negotiations on OECD membership. Latvia has continued its successful recovery after a dramatic economic downturn and negotiated favourable growth-oriented conditions under the new EU Multiannual Financial Framework. The preparations for Latvia's Presidency of the Council of European Union started in earnest in 2013. At the same time, NATO demonstrated its presence and credibility in the Baltic Sea region by holding the largest military exercises to date.

The economic difficulties of the previous years contributed to an increased understanding of and practice of using foreign policy as an instrument for societal performance and welfare. This has led to a gradual economisation of Latvia's foreign policy and also manifested itself in economic diplomacy endeavours in 2013. Latvia has cooperated closely with the United States and other Euro-Atlantic partners on the effective operation of the Northern Distribution Network to Afghanistan. The attempts to establish closer and potentially mutually beneficial economic relations with Central Asia, India and China became obvious. In a similar vein, the Latvian government has demonstrated its willingness to engage with Russia, establish a pragmatic relationship and intensify its trade and investment links.

Latvia's external eastern vector has not only provided windows of opportunities but also revealed the existing concerns and potential challenges. It proves to be a complicated task both domestically and internationally to ensure an acceptable balance between values and interests in foreign policy statements and practice, especially with regard to some of the former Soviet republics. The intensive and positive economic interaction between Latvia and Russia notwithstanding, the military exercises in the region, as well as informational and historical "football", reminds us of the uneasy nature of bilateral relations. Moreover, Russia's selective trade sanctions against Latvia's Baltic neighbours and Eastern Partners, especially Ukraine, demonstrated the existence of competitive integrationist projects in

the post-Soviet area. This provides a challenging setting for Latvia's foreign policy choices and activities in the context of the Eastern Partnership initiative and its planned Summit in Riga in May 2015. Moreover, the European and national elections in 2014 will create additional political exigencies for decision makers.

The Latvian Institute of International Affairs launches its first annual Foreign Policy Yearbook to address the very issue of continuity and change in Latvia's foreign policy. Although this analytic endeavour brings together authors with a diversity of backgrounds, we are united in our willingness to facilitate the understanding of the place and tools of a small country in international affairs. This publication reflects on the major foreign policy vectors, outlines views on prospective developments, introduces additional themes and provides policy recommendations. Hence, the Foreign Policy Yearbook contributes to and, we believe, enriches an informed and thorough debate among the decision-makers and the general public on the Latvia's foreign policy priorities, challenges and windows of opportunities.

EUROPEAN INSTITUTIONAL ADJUSTMENTS AND THREE CHOICES AND PERSPECTIVES FOR LATVIA AND ESTONIA

Viljar Veebel¹, Kārlis Bukovskis

The current financial and economic problems in the European Union and the eurozone in particular have resulted in multiple existing and upcoming institutional changes in the EU. Many have been asking whether Europe's future requires only a deepening of integration. The repatriation of competences, diverging attitudes towards the Fiscal Compact, the Banking Union, the eurozone, the European patent with unitary effect, the social dimension of the Economic and Monetary Union, the Fiscal Union and many other "more complete" plans of the European Union are questioned not only by a British review, but also by Dutch subsidiarity inquiries and Germany's acknowledgment of the possible repatriation of powers from Brussels. All of these issues are perpetually discussed not only among politicians and the academic community, but also among journalists and the general public in the countries. Thus, this article has chosen to deal with the current European ideational and political uncertainty from the conceptual point of view of two small eurozone member states: Estonia and Latvia.

The hope and illusion that European integration is a well-built mechanism, leading seamlessly to economic welfare and political harmony, has been lost and cast away in recent years. In light of the financial crisis, the European Union's institutional system and governance quality has been a target for criticism from the public, economic actors, the media and academia, which indicates a wide gap between the expectations of society, the legal competences and institutional decision-making mechanisms. What are the problems that need to be overcome both theoretically and in practical policy-making for small member states – specifically Latvia and Estonia – in this process? What is there to be gained or lost different reform scenarios? After a concentrated conceptual evaluation of three viable choices for states in developing the EU further, this article will analyse 2013/2014 debates and perspectives in Estonia and Latvia. Using policy documents, statements and expertise from previous research, the authors will identify the trends and the perspectives that local societies look for and politicians provide.

The list of challenges and necessities is long – most of them have been initiated from fiscal imbalances, but they also reflect institutional problems in the EU. The lack of transparency in terms of member states' fiscal obligations, insufficient scrutiny by the European

¹ Estonian National Defense Academy

Commission and the European Central Bank, an absence of clear norms and convincing sanctions, and the inability of supranational institutions to regain control over widespread member state violations of the Maastricht criteria are some examples indicating the need to reform the legal and institutional system of the European Union. But the choices and perspectives of member states in terms of a new institutional structure, the legal model and power division differ: while some prefer to renovate the existing community model of functional integration, a second group supports federalisation and a third group prefers the so-called stakeholder model.

Instead of an idealistic debate, the options concerning institutional reform should be based on measurable results, rational argumentation, open debate and inclusion. Idealism, optimism and solidarity are some of the incentives for European cooperation, but not necessarily the best baseline for building an economically competitive and fiscally sustainable Europe in the long term. In the process of debate and selection there is also no need to underestimate the critics of the federal, functional or stakeholder models as they help to find potential bottlenecks and therefore throughout the debate improve the end-result. This means that the national competence in assessing the developments of institutional reforms must increase among civil servants, academia, the media and the public.

The first choice: federalisation

The general aim of federalising reform would be to gain more administrative and political control over member states' fiscal policies, consolidate already-conducted reforms in the financial sector and reach a fundamentally new qualitative level of the European Union unification process. But it is also clear that federal reforms will not help to improve EU competitiveness, bring more funds to the EU budget or increase exports. Accordingly, the dominative hope among federalisation supporters – that more Europeanisation, cooperation and centralised scrutiny adds efficiency – has not been proven scientifically.

In which way would a federal Europe differ from the current institutional logic and legal principles? In an ideal model, federal reform would bring a clear, standardised, fixed, legally binding and stable political and institutional balance of power between the EU institutions and the member states with mechanisms that provide additional scrutiny and coercion. In practice, a federal relationship ought to create a situation in which problematic member states would not be able to abuse joint resources and solidarity to solve their debt issues by transferring the responsibility and the cost to the shoulders of other member states. It would also be clearly stated which competences are delegated to the federal level and which would remain for national governments.

Federalisation would force Europe to achieve stability through the uniformity of all member states despite their differences in terms economic development, geographic location and social traditions. This would, at least in short run, improve the financial health of the union and the states in debt, but with the expense of slowing down the

development of the stronger members. As a result, the EU as a union would in the future be less able to use its special advantages.²

The main problem with federalisation is that it contrasts with the existing model of functional integration.³ First, the existing model also allows membership in the union for states⁴ that do not want to participate in all common policies. Second, the existing model allows the flexible combining of supranational and intergovernmental institutions.⁵ Third, if a federation would bring member states less control over agenda and less competence control, what would be their interest in supporting this process?⁶ This concerns mainly the interests of big member states, whose representation in a federal model would probably be worse than in a stakeholder model or in the existing division of votes and seats.

The idea of federalisation has many supporters among the Estonian political elite,⁷ because it is seen as an alternative to a multi-speed of Europe in which the Baltic States would classify as periphery, with all the security concerns and a decline of economic advantages. It is also believed that small and peripheral states are better able to defend their interests in a federal union.⁸ Based on those arguments, the EU policy of the Estonian government has been supportive of the federalisation of the EU.⁹ In Estonia, federalisation is seen as possibly the best alternative to counter-balance the big member states' dominance in terms of Council voting and their financial impact in the European Stability Mechanism. In legal terms, federalisation demands an additional mandate from citizens at a referendum, to ensure long-term legitimacy with regard to the EU.¹⁰ A referendum would also initiate wider and more active public debate on European institutional reform. Federalisation has not been openly debated in the Estonian media. There have been numerous articles advocating for federalisation, but there is a lack of comprehensive and reasoned criticism or a sound dialogue between the protagonists and antagonists.¹¹

For small states, the federal model offers both possible dangers and advantages when compared to other possible reform scenarios. The threats are connected to effects of centralisation and unification, which reduce small states' ability to use their specific advantages. Also, federal legislation tends less to reflect the peripheral problems of small states than the needs of big states in the core of Europe. The advantages are related to guaranteeing levels of representation, participation and inclusion, which at least in some

² J. Kregel, Debtors' Crisis or Creditors' crisis? Who Pays for the European Sovereign and Subprime Mortgage Losses? Public Policy Brief no 121 (Levy Economics Institute of Bard College, 2011).

³ Also known as „community“ model.

⁴ United Kingdom, Sweden, Denmark, Ireland etc.

⁵ J. H. H. Weiler, The Transformation of Europe, The Yale Law Journal, Vol. 100, No. 8 (1991), 2403–83.

⁶ Andrew Moravcsik, The Choice for Europe: Social Purpose and State Power from Messina to Maastricht (Ithaca, New York: Cornell University Press, 1998), 35–8.

⁷ Toomas Hendrik Ilves, Ma ei saa aru tondist, mida maalitakse föderalismi ees, Postimees, 14.01.2013.

⁸ H. Rumm, Võib-olla tõesti rahvusriikide föderatsioon?, Postimees, 14.01.2013.

⁹ Government of Estonia, Estonian EU Policy 2011–2015 (2011),

http://valitsus.ee/UserFiles/valitsus/et/riigikantselei/euroopa/Eesti%20EL%20poliitika_EST.pdf

¹⁰ Viljar Veebel and Anastassia Kovalenko, Millisesse Euroopa Föderatsiooni?, Postimees, 08.04.2013.

<http://arvamus.postimees.ee/1195050/viljar-veebel-ja-anastassia-kovalenko-millisesse-euroopa-foderatsiooni>

¹¹ I. Raig, From European Federation and its Alternatives, Proceedings of Estonian Parliament (Riigikogu Toimetised), n27/2013.

institutions overweight the actual size of small states.¹² Federalism also sets some limits to the legal, administrative and cultural “melting” of smallest states, as once again their special competences and representations are safeguarded. Thus, there is the choice of whether to go on as a loosely bound confederative union or to create a federation, but with significantly fewer members that in turn have more common interests.¹³

The second choice: the stakeholder model

The stakeholder model of institutional reform represents a business-based vision of how to prevent fiscal irresponsibility and the abuse of European solidarity to cover national debt in the future.

The central principles of the stakeholder model¹⁴ are already used to design the institutional systems of the ESM¹⁵ and the EFSF¹⁶ – the symbols of future economic and fiscal cooperation in Europe – are economic reasoning, rationality and profitability, the protection of the interests of creditors, confidentiality, the correspondence of member states’ representation to purchased shares, and the complete voting dominance of the majority over the minority according to the distribution of votes.¹⁷ The corporate model that was chosen to govern the ESM and the EFSF is also used in governing the International Monetary Fund. Meanwhile, the core values of today’s European Union’s institutional and legal system are consolidative democracy,¹⁸ a culture of consensus, the inclusion of interest groups, the transparency of legislation, the equal treatment of Member States whenever possible, solidarity and the subsidising of weaker societies, respect for diversity and the support of peripheral areas at the expense of market principles. The stakeholder model is based on institutionalisation logic and the values of a profit-focussed business corporation, while in the existing community model of the EU, on the other hand, is based on solidarity and overrepresentation for smaller member states.

Even though the corporate model of governance of the ESM and the EFSF is in German, French and Italian interests, the best way to solve the financial crisis and conforms better to the principles of a market economy where “the one who pays the bill can also order the music”, it may be questioned whether a 0.186% and 0.255% voting right for a possible 3 billion euro obligation was precisely how a small state like Estonia pictured itself sharing in the solidarity of the EU and participating as an equal nation state in European affairs.¹⁹

¹² In the EU, overweighting is used most in the European Commission and the European Court of Justice, but also in the Council of Ministers and in the European Parliament.

¹³ J. Zielonka, *Europe as Empire: The Nature of the Enlarged European Union* (Oxford University Press, 2006), 35.

¹⁴ R. K. Mitchell, B. R. Agle, D. J. Wood, *Toward a Theory of Stakeholder Identification and Salience: Defining the Principle of Who and What really Counts*, *Academy of Management Review*, 22(4) (1997), 853–88.

¹⁵ Created in 2012 with The Treaty Establishing the European Stability Mechanism (2012), <http://www.european-council.europa.eu/media/582311/05-tesm2.en12.pdf>

¹⁶ Created in 2010 with the EFSF Agreement (2010), http://www.efsf.europa.eu/attachments/20111019_efsf_framework_agreement_en.pdf

¹⁷ The Treaty Establishing the European Stability Mechanism (2012), <http://www.european-council.europa.eu/media/582311/05-tesm2.en12.pdf>

¹⁸ Sometimes seen obsolete and stagnated.

¹⁹ It is also worth noting that in order to gain a 0.186% voting right in the ESM and a 0.255% voting right in the EFSF, Estonia took the responsibility of making a payment of 148 million euros, and as a

Despite the discouraging facts of low representation, Estonia has also been one of the member states in support of the stakeholder model – the idea that state functions may be carried out more successfully by using the corporate model of governance at a European level. In some aspects of fiscal and financial stabilisation, the stakeholder model may have advantages because of its support for net payers, who are also the main subjects for additional future payments for stabilisation. The main supporter of the stakeholder model in Estonia has been Minister of Finance Jürgen Ligi,²⁰ who stressed that this model is both more effective in decision making terms and also more ethical, as it gives the right of decision to those countries who actually pay for policy. This approach has also been openly supported by Prime Minister of Estonia Andrus Ansip.²¹

Of the three choices on the table for institutional reform, the stakeholder model, however, offers by far the smallest representation for small member states with a small GDP like Estonia and Latvia and tends to over represent countries with a bigger population and GDP. Accordingly, the biggest members of the European Union would prefer this model over federalisation or renewing the existing community model.

The third choice: the simplification and reparation of the “community” model

Aside from radical reform plans towards federalisation or a stakeholder model, one option for institutional reform is also the fundamental reparation of the existing community model of functional integration. What are the disadvantages of (or misuses of) the previously successful and traditional integration model, and can these be repaired?

The evolutionary logic of the European Union’s institutional development has been based on the idea of a constant widening and deepening of its competences to new fields and member states.²² The progress of institutional integration is symbolised by increasing institutional bodies, growing budgets, numerous standards,²³ increasing re-distribution,²⁴ subsidies, and the growing regulation of markets. Joint activities and regulation have been seen as something that creates additional value *a priori* and hence needs no additional justification, whether it is in the form of the Common Agricultural Policy, the eurozone or the Schengen Area.

Solutions to overregulation and centralisation have also been searched for in previous decades: to safeguard national needs and interests at a European level, the principle of subsidiarity was upheld in 1980s, according to which European Union institutions first need to prove and explain why and how additional legislation or initiative creates added

shareholder to take obligations for up to 3 billion euros (roughly 2,500 euros per capita), which is almost 50% of Estonia’s central budget revenues in 2013.

²⁰ Stenograph of Estonian Parliament, 27.09.2011, <http://www.riigikogu.ee/?op=steno&stcommand=stenogramm&date=1317107100&pkpkaupa=1&paevako rd=8895>

²¹ Stenograph of Press Conference of the Government of Estonia, 16.06.2011, <http://valitsus.ee/et/uudised/pressikonverentsid/stenogrammid/37712/valitsuse-pressikonverentsi-stenogramm,-16.-juuni-2011>

²² Also known as the spill-over effect, in B. Rosamond, Theories of European Integration (Basingstoke: Palgrave, 2000).

²³ Circa 2000 new regulations, directives and decisions annually.

²⁴ The budget of the European Union grows circa 6-7% every year.

value compared to already-existing national legislation. With the principle of proportionality, it was additionally stated that the joint legislation of the European Union can only go as far as is directly needed for actual policy goals.²⁵

Before the upcoming institutional reforms it is worth asking whether it was the complex institutional system, financial subsidies, the sharing of responsibilities in supranational bodies and the 2,000 new regulations and directives every year that built the welfare and stability in Europe. Or was it a joint and simple system and internal market to serve member states' joint and overlapping regional interests in the fields of economy and security? Originally, the idea of an internal market and customs union was not carried out by rampantly escalating regulation and quieting the market signals, but quite the opposite: easier and unobstructed access to the markets of other member states, which created more open competition, economic growth and security.

That joint activities, growing regulations and re-distribution also have a negative long-term impact has not been reflected much in public debates, although there are some examples of this. First, the unemployment rate in the eurozone is higher than in the member states outside the single currency area. The accumulation of the debts of the countries using the euro (Greece, Portugal, Ireland, Spain and Italy) has, on the other hand, taken place within the conditions of the single currency and the lack individual responsibility. Third, it is precisely the rules of the single currency and the eurozone that have led to the drastic decrease in the productivity of the countries now struggling with debt – they are facing payment difficulties and their labour markets have not been able to adjust. A similar trend may be observed in the Common Agricultural Policy, where seemingly more effective subsidies deepen the reduction in productivity and the loss of competitiveness year-by-year.

This dilemma was a subject for debate already 10 years ago, when the Treaty establishing a Constitution for Europe was being forged. The answer that came up would be very appropriate even today, although very little effort has been made to apply it. It was agreed that upgrading and updating joint legislation and delegating responsibilities to the EU cannot stop, but in parallel a process of active deregulation and returning competences to member states could take place, which would allow them to use their distinctive competitive advantages better. As a bonus, it would allow retaining and increasing the individual responsibility of member states. In practice this would require a permanent working group consisting of representatives of the member states who would select areas and issues that either need regulating on a supranational level or that any joint regulation would bring adverse results to.

In the case of Estonia, the governmental position concerning competences, redistribution and regulation levels has been changing over the past 10 years of membership. In its first years of membership, Estonia supported stronger subsidiarity, deregulation, market liberalisation and the reduction of subsidies.²⁶ Also the intergovernmental model, with the dominance of the nation state policy initiative, was seen as more in line with Estonian interests and values. The political line concerning regulation and competences started to

²⁵ Mostly related with consumer protection and environmental protection legislation.

²⁶ Government of Estonia (2004), Estonian EU Policy 2004-2006, https://valitsus.ee/UserFiles/valitsus/et/riigikantselei/euroopa/eesti-eesmargid-euroopa-liidus/eesti-euroopa-liidu-poliitika-2007/Valitsuse_Euroopa_Liidu_poliitika_2004_2006.pdf

change in 2008.²⁷ Growing regulation and integration was seen as positive and providing social security, while market regulations were seen as failing expectations and needing additional regulations. Principles of the market economy and national responsibility were seen obsolete and were replaced by ideas solidarity and growing the competences of joint institutions. Government representatives also stated that the community model offers the best possible representation for a small state like Estonia.

To sum up, the European integration process has been no doubt successful in fulfilling the two main objectives that were pronounced with its creation – to grant peace and prosperity to its citizens. Therefore, before rushing into fundamental institutional reforms towards federalisation or a stakeholder model it would be worthwhile to modify the existing European Union in a way that would conform to its original ideas – to promote freedom, take advantage of its diversity and invigorate its economy.

Estonian perspectives on picking the best choice

The central variables influencing the attractiveness of the previously described three institutional reform scenarios are the actual level of national representation and influence in institutions, the level of sovereignty to be shared and the amount of returns in terms of security and welfare.²⁸ Both development towards a federal model and deepening the community model were seen in this aspect as useful for Estonia, as these would protect against the growing influence of bigger member states.

The next variable, “actual representation in institutions”, does not only mean the number of votes or seats – for small states like the Baltic States, it is often more dependent on the amount of qualified administrative professionals who can act professionally and decisively on these seats and with these votes. During the almost 10 years of Estonian and Latvian membership in the EU, neither the public, the media nor academia have debated about whether national representation in the EU institutions might be systemically too small. But there have been debates on how to find sufficiently experienced and prepared candidates for high-ranking EU positions within the structures of national ministries, the European Commission and the Council of Ministers.

Throughout previous institutional reforms and renewals of treaties, the positive discrimination towards small member states has always been a central principle to compensate for their actual size. That has been one of the main principles of the European Union as it was created – to work together, in consensus if possible, while taking into account the diversity of the EU. There is no certainty, however, that it will remain so indefinitely. Also, the possible dynamics concerning democracy in EU institutions has found little ground for debates, as in EU institutions Estonia enjoys overrepresentation and its micro-representation in the ESM and in the EFSF is not widely known. What has been communicated more often both in Latvia and Estonia within the past two years is the need to avoid a multi-speed Europe. In case of the emergence of such a state of play, the

²⁷ Government of Estonia (2007), Estonian EU Policy 2007-2011, https://valitsus.ee/UserFiles/valitsus/et/riigikantselei/euroopa/eesti-eesmargid-euroopa-liidus/eesti-euroopa-liidu-poliitika-2007/ELPOL_2007_2011.pdf

²⁸ E. Antola, M. Lehtimäki, Small States in the EU, Working Papers, Jean Monnet Centre University of Turku, no 10 (2001).

positions of both countries have been to ensure that they are represented as core members.

The next variable, the question of gains, has been at the centre of legitimisation debates in Estonia since the beginning of eurozone crisis in 2008, when debates focussed on additional sovereignty sharing, decreasing representation or growing joint rule. Estonian government ministers²⁹ and President Ilves³⁰ have throughout the membership years been in consensus that the gains in terms of security and financial support are so remarkable that generally Estonia is not only satisfied with the current vote distribution, but would be ready to accept any of the previously debated three scenarios, including possible additional payments and reduced representation only in order to keep its membership. Between the government and president, arguments about preferences have been slightly different. President Ilves prefers as much of a federal solution as possible, preferably following American experience, with strong economic and security connections.³¹ But he has also agreed with existing reforms towards a stakeholder model by saying that despite new conditions Estonia receives more subsidies from the EU than it pays to the common budget and therefore it should not complain.

Prime Minister Andrus Ansip and Minister of Finance Jürgen Ligi see the European role in the Estonian economy growing increasingly important and in many aspects irreplaceable. Accordingly, during the debates over the ESM and the EFSF, they have stressed that their central aim during fiscal reforms is to keep eurozone stability and joint solidarity at any cost, as these provide the best possible economic conditions for Estonia in the longer perspective. Their opinion is also supported by fact that European subsidies and investments reached 22% of the Estonian budget in 2012. In general, the Estonian government's position in terms of institutional reforms is most similar to the German position, where the stakeholder model is preferred in fiscal and economic matters and federalisation is preferred as a general concept.

The curious case of public debates in Latvia on the EU

The year 2013 has been a remarkable year in Latvian-EU relations. The year could be entitled “the euro year”, as most of the discussions concerning the country's membership in the EU were tied to the adoption of the Multiannual Financial Framework 2014-2020 and the introduction of euro currency from 1 January 2014. As the final ECOFIN decision was made only on July 9th, the pre-decision and post-decision time is characterised by two diverging attitudes among the political elite and their respective ideational supporters. The pre-decision time was based upon ongoing discussions not only on EU accession, but also on the economic sustainability of the eurozone and the European Union in general. The post-decision era, at the same time, is more definite and allows less speculative discussion on the place of Latvia in the EU, and opens to more decisive discussion on the expected form of the eurozone and the EU in the near future.

²⁹ J.Ligi, Kreeka abistamine on õiglane, Postimees, 11.10.2011, <http://arvamus.postimees.ee/593622/online-vaitlus-kreeka-abistamine-on-oiglane>

³⁰ Toomas Hendrik Ilves, Aitäh ESMiga tehtud töö eest Riigikogu, Postimees, 10.09.2012, <http://arvamus.postimees.ee/967620/toomas-hendrik-ilves-aitah-esmiga-tehtud-too-eest-riigikogu>

³¹ Toomas Hendrik Ilves and J.Raidla, Ilves ja Raidla Euroopa Föderatsioonist, <http://www.eurokratt.ee/ilves-ja-raidla-euroopa-foderatsioonist/>

The Estonian accession to the eurozone triggered similar public discussions back in 2010, with similarly low public support for membership as was experienced in Latvia in 2012/2013. Debates on the economic and even political viability of the eurozone and the European Union as such were discussed not only among experts and academicians, but also among politicians and the mass media. The more reluctant politicians from political parties represented in the parliament expressed their reservations and proposed the postponement of accession until after the EU and eurozone are over their internal economic and political problems. Like in Estonia, the decision was made to go on with the project, which requires not only a political decision, but also the fulfilment of numerous economic requirements. It is clearly stated in the annual report by the minister of foreign affairs on activities performed and planned in national foreign policy and on activities performed and planned in European Union matters that “2013 has been decisive for Latvia’s deeper integration into the EU structures; that firstly relates to the acceptance of Latvia into the Eurozone; Latvia has paved itself in the core of the EU member state cooperation”.³²

At the same time, one should acknowledge that the discursive public discussions in Latvia and to some extent in Estonia are reactionary and often bound to other EU related matters without proper devotion to the discussions on the core values of Latvia’s EU membership. The values and principles that Latvia and its population defines as self-characteristic must be the basis for communication on the future outlook of Latvia and Estonia in the EU. Although it is rather typical for the modern Baltic States to lack immediate political values or traditional political culture characteristics, there is a clear necessity to define these to cement the understanding of the Latvian population about their nationhood and “European-hood”.

The introduction of euro, the presidency of the Council of the European Union, and the discussions on the Multiannual Financial Framework operate as flagship topics in Latvian domestic discourse on EU matters. Individual matters like those previously mentioned appear to have taken over the communication space originally intended for discussions on both the philosophical aspects of country’s membership in the EU and the regular decision making process and pending legislative matters.

Thus, it is essential to realise the opportunity that the previously mentioned report provides for more in-depth discussion in Latvia on the institutional alterations in the EU and the best choices for the small country. The report clearly states that the “EU is the only realistic international relations model in Europe that secures the external environment for democratic development, political stability and sustainable economic growth in Latvia. The EU permanently changes reacting to internal and external challenges. The institutional reforms in the EU are essential for Latvia as an EU member state, in order to facilitate its functioning. Latvia will actively participate further in the EU integration process, emphasising the maximum exercise of its already adopted treaties first”.³³ This statement clearly indicates Latvia’s willingness to remain a part of the EU and facilitate institutional adjustments by piecemeal engineering. Thus, the country, similarly to Estonia, seeks to

³² Ārlietu ministra ikgadējais ziņojums par paveikto un iecerēto darbību valsts ārpolitikā un Eiropas Savienības jautājumos (Ministry of Foreign Affairs of the Republic of Latvia, 2014), 4, http://www.mfa.gov.lv/annual%20report_2401_en.pdf

³³ Ibid.

support the federalisation or stakeholder choices if opting to become a eurozone member state is seen as a defining decision.

The report allows domestic discussions on Latvia's interests on the shape of the European Union and the so-called "red lines" in the EU to take place. Moreover, the perspectives and views dominant among the Latvian politicians are not being shaped only by immediate decisions on the issues on the current agenda or the presentation of the report. Foreign policy analysts, journalists and academicians in both countries are commenting and providing the local population with perspectives on individual issues as well as a general outlook on the future of the EU. What has been lacking, though, is a more coherent or guided discussion on the three options indicated in this article and the institutional, political and economic setting of the EU in general. Two research projects were intended to provide some background for further discussions. First, the Rīga Conference Papers 2013³⁴ dealt with the four scenarios for the EU. Published in English and covering the strategic outlook for the EU as a whole, the publication did not become a corner stone for further Latvian domestic debates, although it provided clearly defined scenarios with causes and consequences for each of them.

The second research, which was presented in November 2013, is based on polling results on Latvian attitudes and wishes regarding the country's membership in the EU.³⁵ The authors of the research came to conclusions on several perspectives dominating Latvia. Firstly, the Latvian population sees the preservation of national identity and culture as well as market protectionism as the core principles for Latvia's further positioning on the federalisation of the EU. Secondly, the trend among Latvian integration supporters is to see federalisation or deeper integration as a logical step in the implementation of Latvia's national interests. Thirdly, businesses tend to support federalisation as a means to achieve a fully integrated market for goods and services, which is not available in the present state of affairs. Last but not least, for most of the Latvian population it is essential to reduce the legitimacy gap between the decision-making level and general population. The research clearly concludes that society wants to be consulted on Latvia's further EU integration plans, as the eurozone accession process created something of a democratic deficit.

Thus, it is clear that in both Latvia and Estonia a purposeful, targeted discussion on the future of the EU is essential. Political and expert debates with a clear goal to define Latvia's values and priorities in the EU are necessary not only for increasing democratic legitimacy and closing the gap between politicians and the population, but also for further communication on EU matters. A well-informed and frank debate would increase awareness of the EU processes as well as allow for defining the core values that both modern Latvia and Estonia exist for.

The year 2013 in Latvia allowed the country to define the strategic choice of membership in the EU. The upcoming presidency of the Council of the European Union will bring up more debates on the costs and benefits of EU membership – these are not the most productive and pragmatic as they are often used for populist purposes by visible officials.

³⁴ T.Kleine-Brockhoff, *Post Crisis: Europe and the World in 2025. Four Foreign Policy Scenarios* (Washington: German Marshall Fund of the United States, 2013), http://www.rigaconference.lv/wp-content/uploads/2013/09/RigaConferencePapers_FourScenariosweb.pdf

³⁵ Ieva Bloma and Mārtiņš Daugulis, *Latvijas nākotne Eiropas Savienības attīstības ietvaros: diskusijas par federālismu un tā nozīmēm sabiedrībā* (Rīga, Latvian Institute of International Affairs, 2013).

Thus, a debate on the shape of the European Union and the eurozone that Latvia would like to be a part of would take euro-scepticism off the table and compliment the debate with a more detailed analysis, more factual information and more EU-level arguments. Discussions on the ideal shape and size of the EU would define the very necessity for the EU as a given.

Conclusions

The European Union's battle with the financial crisis and the subsequent reforms in 2011-2013 have been following a rather unexpected logic. First, there has been an ongoing heated debate on the possible federal future of Europe, with much discussion on ideals and common values, but which has led to no practical results. Secondly, improving the present community model of integration has been quite decisively rejected both in an economic and a political sense, while the politicians who requested such a debate³⁶ have been branded as adversaries to the EU by some. Third, by using the stakeholder model, new financially powerful institutions – the European Stability Mechanism and the European Financial Stability Facility – have been created. Wider democratic participation of the public was found unnecessary even when the created financial funds are several times larger than the EU budget and are governed in a substantially different manner from the legitimate logic of the EU.

Small states have in these developments their own possible advantages, losses and preferences. Based on previous historical experience of institutional reforms, the process will be intricate and face many challenges. If one sees this effort as being in the interest of small states, then a more active and targeted participation impact analysis is needed. From the position of the small member states, it is crucial to map their objectives with regard to European Union institutional reform and then through proactive actions to steer the reform process instead of adjusting their behaviour to the positions of other member states by reacting to ongoing processes and passed opportunities.

The outcome of institutional reform from the position of the small member states depends on how well their governments are prepared, how well they are able to formulate their objectives and specific starting conditions, find argumentation, and set feasible roadmaps. Successful and proficient participation requires professional homework in the form of thorough research and discussions which involve all stakeholders: politicians, scientists, entrepreneurs and representatives of civil society. The aspects of legitimacy and democracy are important – citizens and interest groups need to be included from the very beginning so that they can claim ownership of the results.

Latvian and Estonian domestic debates on the future of the European Union that both countries have chosen to be a core part of demonstrate their rather similar necessities and needs. Both countries have choices and both countries are in urgent need of targeted domestic debate on the future of the EU to have their political legitimacy and societal acceptance increased. Taking into account the already-happening institutional (and additional sovereignty) reforms because of the Fiscal Compact or eurozone membership and the emerging Banking Union, Estonia and Latvia are in a position to question their own

³⁶ For instance, the UK's Prime Minister David Cameron with his "Speech on The Future of Europe".

perspectives as well. Moreover, the actualised and potential institutional or legal alterations in the EU would be easier to address in both countries with a proper domestic debate. National conventions on the future of the European Union could be an adequate approach for defining the Estonian and Latvian perspectives and increasing public participation. Of course, in the case of Estonia the timeline is less pressuring as is the case in Latvia because of the upcoming presidency, but in both cases this could be administrated by non-governmental organisations and presented as a project prepared by the Estonian or Latvian populations. Thus, a readiness for European Union wide debate is tied to national choices and the perspectives expressed in targeted and non-hasty discussions.

LATVIA'S STABILITY WITHIN THE EUROZONE'S INSTABILITY

Aldis Austers

As of 1 January 2014, Latvia has become the 18th member state of the eurozone, a group of European countries using the single currency euro. Latvia is following in the footsteps of its neighbouring country Estonia, which joined the eurozone already in 2011. Another of Latvia's neighbouring countries, Lithuania, has expressed its intention to join the eurozone in 2015. Except Lithuania, none of the other Central and Eastern European countries that are member states of the European Union but not full members of the Economic and Monetary Union (EMU) have expressed their readiness³⁷ to join the eurozone in the near future.³⁸ Even those member states that had plans to join the eurozone have recently reconsidered their strategy and revoked their previously set target dates for accession.

In this article I will, *firstly*, address the issue of Latvia's membership in the eurozone. What does this membership mean to Latvia, and how much, if at all, does Latvia's membership matter to the eurozone? Will membership in the eurozone help to resolve Latvia's perennial problem of economic underdevelopment? Why are the Baltic countries so eager to become eurozone members, while the other countries from the CEE region have a lukewarm attitude? *Secondly*, I will offer some analysis related to problems with the functioning of the eurozone. Is the situation in the eurozone improving or getting worse? How best to appraise the plethora of arrangements delivered so far? Why is it so difficult to agree on a lasting settlement to the existing problems?

The basic argument is that the membership of Latvia in the eurozone matters both to Latvia and the eurozone itself. However, though it is beneficial in many regards (e.g., greater political influence, the removal of currency risk, better terms for trade and investment), membership will, nevertheless, expose Latvia to a number of fundamental challenges, and without further domestic reforms Latvia risks permanent economic underdevelopment. Latvia will also have to push for further reforms in the eurozone for its own and also for the union's good. At the moment, tensions have eased due the activism of the European Central Bank and improving economic performance, yet the current truce is passing, as the fundamental causes of the recent crisis – like high debts and a lack of solidarity among the members of the eurozone – have not been so far resolved.

³⁷ According the Treaty on the Functioning of the European Union, every member state, except the United Kingdom and Denmark, has the obligation to become a full member of the EMU once the accession criteria are fulfilled. During the interim period between membership in the European Union and the eurozone, the member states are treated as participants in the Economic and Monetary Union with derogation.

³⁸ Member states of the EU from CEE are: Poland, the Czech Republic, Hungary, Bulgaria, and Romania.

The logic behind Latvia's membership in the eurozone

The eurozone is an opportunity, but not a solution to Latvia's problems. Formally, the eurozone embodies a high degree of economic and financial integration among sovereign European countries who are members of the European Union. The shared currency makes capital transfers and trade between the member countries much cheaper and less risky. Moreover, as member states cannot resort to competitive devaluations, the common currency creates a more level playing field among economic actors all across the eurozone. And consumers can benefit from a greater choice of goods and suppliers. "One money, one market", runs the slogan of the eurozone.

At the same time, and this is a fact of life, membership in the eurozone carries considerable political significance both internally within the European Union and globally. Firstly, members of the eurozone form the inner core of the complex integration processes of European sovereign states. For security reasons, Latvia has been striving for the fullest possible membership in Western economic and political structures since the reestablishment of independence in 1991. This unconditional integration has also been seen as a manifestation of the Western cultural affinity of Latvian society. Secondly, the acceptance of Latvia as an equal member of the eurozone raises Latvia's political clout on the world stage. The euro is the second most important currency in the world, after the United States dollar. Around one-quarter of world currency reserves and international debt is held in euros. The euro also accounts for 20% of world currency transactions.³⁹ The ongoing problems of the eurozone have weakened the euro's appeal on world markets; nonetheless, the euro market still remains large, deep and liquid – something that Latvia's financial operators have always envied.

For Latvia, membership in the eurozone also makes economic sense, taking into account the high degree of Latvia's openness to the international flow of goods, capital, and also people. Thus, in 2012, Latvia's net international investment position stood at minus 65% of Latvia's GDP, suggesting Latvia has a very high dependency on inward foreign investment; the share of trade in goods and services amounted to 124% of GDP; and the cross-border migration of people totalled 3.4% of the Latvian population. These figures are comparable to those of Latvia's neighbouring countries, Estonia (which joined the Eurozone in 2011) and Lithuania (which plans to join the Eurozone in 2015); however, they stand in marked contrast to those of other EU member states with an obligation to join the eurozone, like Poland, Sweden and Bulgaria (see Table 1). This is one of the explanations of why the Baltic countries are so keen for euro membership.

Another reason is related to the smallness and openness of the economy. For Latvia, and also for the other Baltic countries, the fixed exchange rate has been a central element of economic policy since 1994. It was like a mantra, zealously defended by the Bank of Latvia. The argument has been that for small and open economies like Latvia, with a high export and import component in the economy and where a single capital transfer transaction can have a considerable impact on the exchange rate, the best option is to follow a fixed rate policy for the sake of domestic market stabilisation, even at the cost of high inflation or deflation. Besides, foreign investors were not keen to accept assets denominated in Latvia's national currency; hence, a fixed exchange rate with a hard peg helped to make the

³⁹ The international role of the euro. European Central Bank, July 2013.

national currency freely convertible and attract investors to Latvia. After Latvia's accession to the European Union in 2004, the early introduction of the euro was seen as a natural continuation of this hard currency peg policy.

Latvia's road to the euro was rather bumpy. Because of high inflation, and then because of a high fiscal deficit, Latvia did not qualify for membership and had to postpone its target dates for accession several times (initially 2006, then 2008, 2010, and, finally, 2014). While on its way to the euro, Latvia saw giddy economic success (nominal GDP grew by 30% from 2006 to 2007!), and also with a rarely seen economic slump, erasing a large part of the pre-crisis economic success. Latvia was forced to ask international bail-out assistance and accept stark fiscal austerity measures. In fact, euro introduction in 2014 was declared as one the objectives of Latvia's stabilisation programme during the crisis. Membership in the eurozone was seen as a vindication and also a reward for Latvia's harsh adjustment and reform effort.

However, there was also a gloomy side to the pursued fixed exchange rate policy. In their aspiration for early euro introduction, the Latvian authorities prematurely equalised the status of euro with the national currency in domestic transactions (the legal tender remained lats – however, the banks could freely, without any restrictions, accept deposits and issue loans in euros). In 2005, when the government's lack of ambition to implement measures to reduce soaring inflation became evident, and it was clear that Latvia would fail to qualify for eurozone membership, the *de facto* status of the euro as a domestic currency was, regrettably, not revoked. This fostered an excessive inflow of foreign funding, overheating and hard lending. With hindsight, it was a very risky policy to accept the euro in domestic transactions to the extent that it nearly replaced the national currency.⁴⁰ The hard peg of lats against the euro was defended using the official foreign currency reserves of Latvia. At moments of distress, the Bank of Latvia could rely only on bilateral currency swaps with other regional central banks. The ECB instruments for banking stabilisation and currency interventions were not available at that time, as Latvia was not yet participating in the eurozone.⁴¹ Ultimately, Latvia paid a due price for that blunder.

	Trade openness (% of GDP)	Net international investment position (% of GDP)	Total population change (% of population)	GDP per capita in PPS (euro area = 100)	Foreign currency loans* (% of corporations/households)
Bulgaria	135	-85	-0.6	41	25/38
Latvia	121	-72.5	-1.4	47	90/90
Lithuania	157	-52	-1.6	53	77/70
Poland	91	63.5	0.0	58	25/38
Sweden	92	-7	0.7	115	12/0

Source: Eurostat, *EC Convergence Report 2010 (data from 2009)

Now the euro has officially become Latvia's currency and the ghost of currency devaluation is gone forever. Despite past mistakes, this is an accomplishment for Latvian policymakers,

⁴⁰ In Latvia, the rate of foreign currency loans issued to households and businesses approached 90% in 2009.

⁴¹ Andres Åslund and Valdis Dombrovskis, *How Latvia Came Through the Financial Crisis* (Washington DC: Peterson Institute for International Economics, May 2011), 47.

especially for the reason that the simultaneous attainment of all the Maastricht criteria – price and exchange rate stability, and stable public finances – has proved a very tricky exercise for quickly growing economies. The so-called “convergence play” has to be blamed for this. The rule is that the closer to membership in the Eurozone a country is, the more attractive the respective country becomes to foreign investors, and hence the more difficult it is for the authorities to control price and exchange rate developments. Moreover, the price criterion for the euro membership has become more and more stringent with every round of EU enlargement.⁴² For that reason, the window of opportunity for price stability consistency has considerably narrowed, and, if Latvia had missed it this time again the country would have had to wait for another recession to qualify.

Yet there is little room for relaxation, as participation in the eurozone will expose Latvia to another set of challenges. First, as the currency risk has disappeared, governmental and private actors might be tempted to borrow more (and financial markets more tempted to loan) than before Latvia’s accession to the eurozone. Second, a narrow labour market makes Latvia’s business cycle shorter and economic growth more volatile than in bigger members of the eurozone. Therefore, the one-size-fits-all monetary policy of the ECB will not correspond to Latvia’s development cycle for most of the time. Third, as a consequence of this, fiscal measures will remain the only effective tool in the hands of the government to smooth out growth cycles. The fiscal organisation will need to be flexible and receptive to market signals. Yet there are limits to this flexibility, as fiscal measures, like taxation, take time to implement. Most likely Latvia will need to build large fiscal buffers and make fiscal decision-making more technocratic (this has already happened with the establishment of Fiscal Council). This will, however, imply less public investment and less remit for democratic discretion.

The listed challenges will be compounded by the following three perennial problems for Latvia: (1) the low level development (Latvia’s income level stands only at 58% of the eurozone’s average); (2) the low level of foreign direct investment accumulation (46% of GDP, while in Estonia it is 87%); and (3) the high level of unemployment (in the long-term it is close to 8% of all economically active people). Besides these problems, some characteristic features of Latvia’s economy have been deep and widespread social problems (around 40% of the population is at risk of poverty), the prevalence of the grey economy (according to some estimates, up to 38% of GDP), and huge regional disparities (the Riga region delivers 67% of GDP).

In the context of eurozone accession, one of the arguments used to raise public support for the introduction of the euro (public support for the euro changeover has been rather modest – around 45%) was the chance for Latvia to become more attractive to foreign investors. This argument has been misguided. As has been already noted above, Latvia has a very low level of accumulated FDI in comparison to Estonia, for example. A large part of the investments that flocked in during the pre-crisis boom landed in the financial,

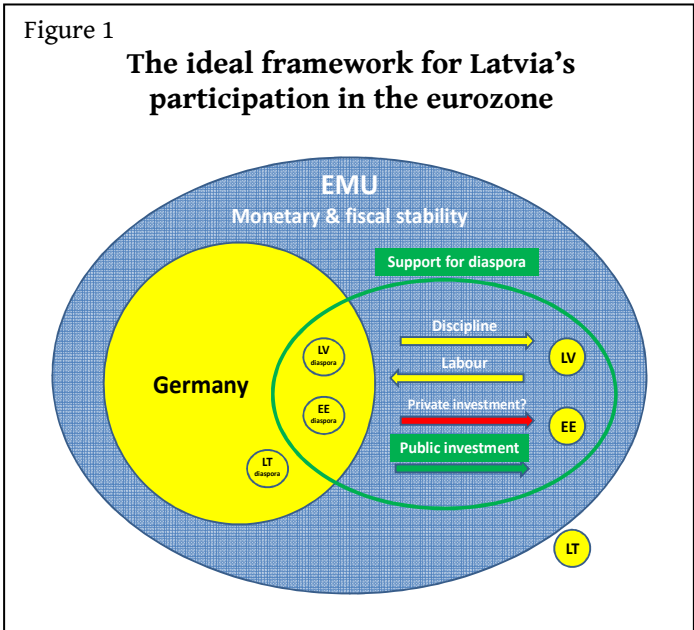
⁴² For more details regarding the problematic accession criteria, see Aldis Austers and Kārlis Bukovskis, “Latvia’s Socio-Economic and Political-Institutional Challenges in the Context of the Euro zone Accession” in *Baltic-German Strategic Engagement: Realignment after the Euro crisis?* (Latvian Institute of International Affairs, Friedrich-Ebert-Stiftung, 2013), http://www.liia.lv/site/docs/StrategyTalks2013_A5_GALA.pdf

construction or retail sectors, leaving the manufacturing sector with virtually no significant investment project realised. Yet this meagre FDI performance happened against the background of very low corporate and capital taxation in Latvia (the third lowest in the EU after Bulgaria and Lithuania) and the fact that the existing businesses in Latvia reap very fat profits (among the highest in the EU). This points to the fact that there exist some other factors which limit the inflow of high quality foreign investment, like unfriendly bureaucracy, corrupt practices, domestic cartels, etc. The IMF⁴³ has stressed the problems with judicial efficiency, the oversight of state-owned enterprises, vocational and higher education, the competition policy, public procurement and the industrial policy.

The demographic decline and emigration are even sexier issues. Low levels of income, high unemployment, social problems and limited opportunities force many young Latvians to leave the country. According to statistics, between 2000 and 2011 Latvia has lost around 11% of its population due to emigration. The exodus continues – in 2012 another 12,000, or 0.6%, has left. This would not be that painful if the demographic balance was positive, but it isn't. As a consequence, Latvia's economy is becoming smaller and smaller, if measured by economically active people. And that, in turn, means less domestic consumption and a thinner labour pool. Under such conditions, it is difficult to see the point of investing in Latvia. It is much easier to invite people to work in factories in Germany and Great Britain. Yet as more people leave, the more costly it gets to run the country for those who stay.⁴⁴

Complex transformations are awaiting Latvia. The shortage of labour will put pressure on the growth of wages. If not matched by productivity growth, e.g., through new capital

investment and the application of new technologies, such development will force a large number of existing businesses to go under, thus creating conditions for a new wave of emigration. Only the presence of significant EU interests in Latvia will be capable of breaking this vicious cycle. By EU interests I mean solidarity policies – assistance to depopulated regions, the promotion of cohesion of development and income, etc. In fact, many of these policies already exist, but they are currently underfinanced.



If public money from the Union's solidarity funds does not compensate for slack private capital inflows, then Latvia and other poorer regions risk getting trapped in a state of permanent underdevelopment. Yet the chance to establish such a solidarity compact is much greater among the eurozone countries. If Latvia decided to stay outside the

⁴³ Republic of Latvia: Selected Issues, IMF Country Report No. 13/29, January 2013.
⁴⁴ C.f., Olivier Blanchard et al. Boom, Bust, Recovery: Forensics of the Latvian Crisis, Final Conference Draft to be presented at the Fall 2013 Brookings Panel on Economic Activity, September 19-20, 2013.

eurozone, it would have to accept a market centred version of the EU, as proposed by the United Kingdom and Sweden. Latvia in such a Union would be a loser. Besides, from the Latvian (as a small nation) perspective, the European solidarity compact should include not only fiscal solidarity, but also elements of cultural solidarity, in the sense that people who move across the eurozone area are encouraged to maintain and pass to their children their national identity. For that purpose specific facilities should be developed, e.g., mother tongue training programmes. A schematic diagram of such a solidarity compact is depicted in Figure 1.

Latvia's membership matters to the eurozone's image. Latvia's economy is a pigmy when compared to the rest of the eurozone; therefore, there will be virtually no economic effect from Latvia's accession to the eurozone on the eurozone's economy. With a population of 2 million people, Latvia's GDP makes up only 0.24% of the whole pot.

However, Latvia's accession carries some political significance. First, the eurozone needs to demonstrate that it continues to be open to further expansion. With Latvia's accession there was no change in voting rules. But the next expansion will trigger a rotation system by which the group of the largest member states will, in fact, regain some of the power diluted away through successive enlargements. Secondly, the recent financial calamities have weakened the image of the euro and the eurozone. The eurozone badly needs good stories and Latvia represents one of these. The enlargement with Latvia is celebrated as "an endorsement of the battered currency".⁴⁵

Typically small countries like Latvia elicit little interest from international financial commentators. Nevertheless, Latvia has been an exception to this rule, and Latvia's economic development and frantic aspirations to join the eurozone has been a subject of fascinating debate among the leading scholars of contemporary economic thought. Latvia was a good pupil from the perspective of the policy preferences of the eurozone's master country, Germany. The story runs like this: Latvia followed austerity policies, consolidated public finances, restored external competitiveness, and returned to a healthy growth path. Thus, Latvia serves as an exemplar of the righteousness of fiscal discipline.

Moreover, Latvia's economy is in an enviable state from the perspective of some other member states. In 2014, Latvia will evince the highest growth rate (+4%) among the member states of the eurozone. The country's unemployment level will continue to plummet, inflation will stay at a moderate level for some years ahead, and public debt will nose-dive.

Germany is certainly looking for more member states that hold similar views. Latvia seems to be a good partner. The problem is that Latvia's economic weight is miniscule. Supposedly, Germany would have preferred Poland over Latvia, as the latter would have brought more counterweight to France. But Poland so far has made no plans to join the eurozone; therefore, "something is better than nothing." Besides, Latvia's political strength weighs as much as Germany's or France's in the Eurogroup.

⁴⁵ Voting rights at the ECB – new club rules, *The Economist*, 14th December, 2013.

The persistence of economic and political challenges in the eurozone

Economic calamities are bound to continue due to austerity policies and the stringent monetary policy of the ECB. A spectrum of problems has continued to haunt the eurozone in 2013, albeit to a lesser extent than in 2012. The feeling of an imminent catastrophe had receded, yet such legacies of the crisis as deleveraging (the settlement of debts), financial fragmentation (interruptions in credit flows between southern and northern regions), elevated uncertainty (a lack of resolute action) and rebalancing needs (fiscal consolidations) have undermined growth in the eurozone. In 2013, eight out of 17 member states suffered from a recession. The eurozone's economic situation is expected to improve in 2014.⁴⁶ This is hardly a success, because, first, the eurozone's growth will lag behind the overall Union's growth rate, and second, the aggregate figures mask substantial differences between the member states.

The relatively calm in markets during 2013 was the result of the bold steps taken by the European Central Bank in 2012. The reorganisation of the Spanish banking system and the partial restructuring of Greek sovereign debt in 2012 also contributed to a better investment environment within the eurozone. Yet a number of new hotspots of problems appeared in the course of 2013. First, Cyprus joined the ranks of those countries needing a bail-out. The haircuts on Greek sovereign debt caused a collapse of the Cypriot banking system, whose assets measured 800% of the Cyprus GDP. Yet another hotspot turned out to be Slovenia. Although no assistance has been requested so far, the economic crisis and careless crediting has wiped out the equity capital of Slovenia's major (state owned) banks.

The economic situation in Greece continued to worsen. Its GDP shrank by a further 4%, unemployment reached 27%, the budget deficit widened to 13%, and public debt hit 176% of GDP, a figure very likely out of reach for repayment without another haircut exercise. It is important to note that the IMF has acknowledged a mistake in its calculations of the impact of austerity measures on the Greek and Portuguese economies. The admitted scale of mistake is considerable, and that implies that both countries should have been given more extended time for fiscal consolidation.⁴⁷

The good news was that Ireland had exited its bail-out programme and returned to the financial markets. Yet growth prospects are frail, and its public debt is bound to increase further, beyond 120% of GDP, due to the banking system's needs and elevated unemployment. It has to be noted that the ultra-low taxation policy of multinationals contributes very little to the stabilisation of its public finances. Besides, the long-term prospects of the country are undermined by the massive emigration of young Irish people. Portugal had also achieved good progress in stabilisation, even though it was still dependent on bail-out funding. Portugal hopes to return to debt markets in 2014, although the situation remains fragile due to soaring public debt. Better export performance has not been able to spur economic growth, which would generate tax revenues enough to reduce the public debt, which is already exceeding 120% of GDP.

⁴⁶ European Economic Forecast. Autumn 2013. European Economy 7/2013, European Commission, 2013.

⁴⁷ IMF Admits It Underestimated the Fiscal Multiplier, Blog posting on Eurointelligence webpage, <http://www.eurointelligence.com/news-details/article/imf-admits-it-underestimated-the-fiscal-multiplier.html>

As for the big economies, Spain should be credited for cleaning up its bad banks and implementing considerable reforms in the public sector and labour market. Despite high unemployment (close to 26%) and growing public debt (around 100%), manufacturing has revived and exports have been booming, sending good news about the prospects of yet-to-be-seen growth. At the same time, reports from France and Italy, the second and third largest economies in the eurozone, have been downbeat. Their economic situation has worsened, raising trembling concerns about potential hard to digest bail-outs in the future. Despite falling growth rates and rising imbalances in areas like unemployment, public debt and the current account deficit, both countries have remained averse to fiscal consolidation, intransigent on reforms, and have spent most of their energy on internal political discord. The economies of the Netherlands and Finland, in turn, have experienced a double-dip recession.

The ECB has few instruments at hand to ease the existing stringent monetary conditions. Contrary to member states' governments and other European bodies, the ECB has proved to be capable of delivering decisive and radical actions. Thus, it has been providing substantial funding to commercial banks at low-interest and with extended maturity (Long-Term Refinancing Operations [LTRO]) since 2008. Moreover, in October 2012, the ECB pledged, if necessary, to buy unlimited amounts of distressed government bonds (the so-called Outright Monetary Transactions programme). These programmes have effectively averted the eurozone from a general credit crunch and break-up. However, such ECB activism has been harshly criticised by the Bundesbank, on the grounds that the ECB assumes too much risk and that it performs monetary financing, which is explicitly prohibited. The ECB has retorted that these programmes complied with its mandate to maintain stability in the system and that they had no impact on price stability.

On the other hand, the ECB is well known for its conservative approach to monetary expansion.⁴⁸ In contrast to the Federal Reserve System, the ECB has been slow to cut the official policy rate, despite the recessionary state of the economy. The exchange rate of the euro against other major world currencies appreciates, notwithstanding the eurozone's troubles. Core inflation⁴⁹ has, in the meantime, hit a historically low level since the inception of the euro (at 0.8 percentage points in 2013). This points to excessively rigid monetary conditions in the eurozone compared to partner regions. This has been hurting European export businesses and economic growth, which is suppressed by financial arrears.

The problem is that the ECB has already adopted a very low policy rate (of 0.25 percentage points since November 2013). If inflation continues to fall, the ECB will have very little room to manoeuvre, and, possibly, will have to resort to quantitative easing – buying bonds from governments with the purpose of stirring up the money supply. Such an approach has been adopted by the Federal Reserve, but would be unconventional for the ECB. For sure, such “wild” money printing would provoke more outcry from Germany, whose housing market has already started to bloat.

⁴⁸ According to its statutes, the ECB's primary objective is to maintain price stability in the eurozone. The ECB defines price stability as an inflation rate below, but close to, 2% over the medium term.

⁴⁹ A measure of inflation that excludes certain items that face volatile price movements like food and energy.

Illiquid bank assets and huge private debts inhibit credit flows and economic growth. Throughout the euro crisis, the usual remedy prescribed to countries with difficulties has been fiscal consolidation and structural reforms. Reductions in public debt have been seen as detrimental to a return to growth, as too much debt diverts resources away from investment. Moreover, leaner wages and prices would restore lost competitiveness, spurring export led growth.

However, out of the six eurozone countries forced to apply for assistance only Greece could be accused of lavish public spending. The other countries were crippled by the necessity to bail-out their commercial banks, be it Anglo Irish Bank in Ireland, Bank of Cyprus in Cyprus, or Parex Banka in Latvia. All of these banks had accepted risky securities and deposits on their books and had issued too many low-quality loans to households and businesses.

Recent research from the IMF suggests that high private debt could be more detrimental to growth than high public debt.⁵⁰ The figures of private debt of some eurozone countries are rather shocking. In the Netherlands and Malta it is close to 220% of GDP, and it is also high in the four countries that have been bailed out: in Cyprus and Ireland it is over 300% of GDP, in Portugal it is 255%, and in Spain 215%. In fact, a high level of household debt is considered to be the main cause for the recent recession in the Netherlands.

So far little attention has been paid to measures that would neutralise the impact of different sorts of excessive private debt (e.g., of households, corporations, or banks). The unpalatable truth is that the more wages and prices are squeezed, the harder it is for weak countries to repay their debts. On the one hand, effective and quick insolvency procedures would help to get rid of excessive debt. But the problem is that due to a cultural stigma, insolvency as a solution is more difficult in Europe than, e.g., in the USA. Another way to reduce the debt burden is to increase income. This could be achieved through either Europe-wide growth enhancing activity, like the deregulation of service sectors, or Europe-wide infrastructure projects, or printing money. A fact of life is that none of these options have been considered viable, as all of these would contradict the existing austerity orthodoxy.

Another aspect of the debt story is that the majority of private debt sits on the books of commercial banks. Banks play a particularly important role in the European economies as suppliers of money resources. However, six years since the start of the financial calamities the woes of the European banking sector have not yet been resolved. Banks still own too much debt, but nobody knows exactly how much and which are the bad banks. In such circumstances banks are hesitant to loan money to each other. The flow of funding towards banks in southern region has dried up and these banks can survive only thanks to financing from the ECB. The European banking system urgently requires cleaning-up. The governments of the EU have carried out stress tests on banks on several occasions.⁵¹ Yet, contrary to the USA, the European results have been repeatedly fudged, as governments were not willing to disclose the real state of affairs of their leading banks.

⁵⁰ Debtors' prison: The euro zone is blighted by private debt even more than by government debt. The Economist, print edition, 26 October 2013.

⁵¹ These tests were meant to find out the true scale of losses of banks, determine the resilience of banks to further shocks, and ask the banks either to underwrite more capital or apply for a winding-up.

This has had two perverse effects. First, instead of fencing off bad assets from good assets, the eurozone itself has been effectively split into two parts, as noted above. This limits the access of households and businesses from the southern regions to credit – e.g., they are charged higher rates of interest in comparison to their northern peers (for similar small corporate loans in Germany and Spain, the difference could be as wide as 3-4%).⁵² Secondly, curiously enough, the German government has been among the most ardent opponents of more transparent bank tests. Some of the German regional “landesbanken” are suspected of having considerable exposure to Greek assets. By providing funding to Greece, Germany allegedly was bailing-out its own banks, a frustrating fact to both the Dutch and the Finns, who were also obliged to donate but whose banks had little to gain.

Designs for a genuine economic and monetary union have been consistently played down. The architecture of the EMU has serious faults. The monetary union has not been matched with a fiscal or a political union. As a result, there are virtually no instruments like fiscal transfers which would equalise the impact of a one-size-fits-all monetary policy for the eurozone’s regions with differing growth cycles. According to a study of the IMF,⁵³ the originators of the EMU made the false assumption that the eurozone would face only moderate country-specific shocks, made rare by a common commitment to fiscal soundness (embodied by the Stability and Growth Pact). The actual development of the EMU, however, showed the elusiveness of this commitment – even Germany transgressed the rules of the SGP amidst its internal restructuring in 2003. As a result, a combination of domestic fiscal and banking risks had been admitted, together with extensive financial linkages between countries. All this turned country-specific shocks into systemic ones, without any mechanism in place to deal with such shocks.

According to a theory of optimum currency areas,⁵⁴ a successful currency union (in an economic sense) requires that the countries sharing a single currency have openness to capital mobility across the whole region, flexibility of prices and wages, and also similar business cycles. This allows the shared central bank to promote growth in downturns and to contain inflation in booms using a single monetary policy. However, in reality these essential conditions are difficult to achieve (linguistic, cultural and institutional barriers limit the movement of people; prices and wages are rigid; and business cycles are difficult to synchronise due to uneven technological development). Therefore, a risk sharing system in the form of taxation redistribution needs to be installed too, with the aim to reallocate money to areas which have been adversely affected by economic shocks. For example, in the United States of America the federal government does not accept responsibility for the debts of individual states. At the same time, federal institutions provide significant fiscal support and risk sharing across the United States even in case of financial distress at the state level (e.g., through deposit insurance, unemployment benefits, etc.).

⁵² Michael Steen, Eurozone SMEs struggle to Access finance, Financial Times, 1st April, 2013.

⁵³ Céline Allard et al., Toward a Fiscal Union for the Euro Area, IMF Staff Discussion Note SDN/13/09, September 2013.

⁵⁴ The theory of optimum currency areas was pioneered by economist Robert Mundell and describes the optimal characteristics for the merger of currencies or the creation of a new currency like the euro.

In June 2012, the Big Four⁵⁵ presented to the governments of the member states a series of reform proposals regarding EMU governance. Under the title “Towards a genuine economic and monetary union”, these ideas comprised the creation of a fiscal, economic, banking and also a sort of political union. The four basic building blocks for a “coherent and complete architecture” were as follows:

- An integrated financial framework (a banking union with the responsibility for supervision at the European level, and common mechanisms to resolve banks and guarantee customer deposits);
- An integrated budgetary framework (a fiscal union with common debt issuance and different forms of fiscal solidarity, a central budget);
- An integrated economic policy framework (an economic union with convergence in areas such as labour mobility, taxation and financial support strengthens the political and administrative capacity);
- Ensuring the necessary democratic legitimacy and accountability of decision-making within the EMU (a sort of political union with a focus on building public support for Europe-wide decisions and inter-parliamentary cooperation).

The June proposals of the Big Four were not met with much sympathy from national governments. Under their pressure, the proposals were redrafted and resubmitted to the governments in December 2012 in the format of a roadmap. The roadmap consisted of the following elements:

- Stage 1 (late-2012 and 2013) - ensuring fiscal sustainability and breaking the link between banks and sovereigns (stronger fiscal surveillance and a partial banking union);
- Stage 2 (2013-2014) - completing the integrated financial framework and promoting sound structural policies (finalising the banking union with common resolution authority and a mechanism for *ad hoc* structural assistance through “contractual” arrangements);
- Stage 3 (post 2014) - improving the resilience of the EMU through the creation of a shock-absorption function at the central level (the rest of the bold measures).

As can be seen from the two submissions, the most essential elements of the original plans have been postponed to an unknown future. What’s more, progress with regard to the implementation of the proposed roadmap has been rather mediocre in 2013.

The Fiscal Union. The initial idea was that the Fiscal Union would consist of two pillars: one of greater discipline and one of solidarity. The solidarity pillar now has been abandoned. However, with regard to fiscal discipline a myriad of new procedures have been erected (“Six-pack”, the Fiscal Compact, “Two-pack”, European Semester, etc.). The most potent instrument is the Fiscal Compact.⁵⁶ In the eyes of Wolfgang Münchau, a commentator for

⁵⁵ Big Four: Herman van Rompuy (Presidents of the European Council), Manuel Barroso (President of the European Commission), Mario Draghi (President of the ECB), Jean Claude Juncker (President of the Eurogroup).

⁵⁶ Formally, the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, also referred to as TSCG or more plainly the Fiscal Stability Treaty, is an intergovernmental treaty introduced as a new stricter version of the previous Stability and Growth Pact. The Fiscal Compact was signed on 2 March 2012 by all member states of the European Union (EU), except the Czech Republic and

the Financial Times, this is a “vehicle to deliver permanent austerity by forcing countries to pay down their excessive debt for 20 years”.⁵⁷ The idea behind all this activity is to arrest the practice of “free-riding” by member states’ governments and to correct significant economic imbalances. The effectiveness of other instruments will have to be tested. Thus, the French have already refused to accept Brussels’s recommendation for structural reforms. The German case of an excessive current account surplus (6.4% of GDP in 2013, while the new rules allow only for a 6% surplus) has been subjected to in-depth review by the European Commission. A verdict is expected in April 2014. Theoretically, Germany could be fined if it refuses to apply measures diminishing this imbalance. Whether this will happen and who will take the upper hand – Berlin or Brussels – remains to be seen.

The European Stability Mechanism. This is the bailout fund for member states of the eurozone. It was established as an international organisation outside the EU framework in September 2012. The ESM replaces the defunct European bailout instruments,⁵⁸ and the rule is that only the countries which have ratified the Fiscal Compact are allowed to benefit from this solidarity mechanism. So far, out of available 500 billion euros under the ESM, 100 billion have been loaned out to Spain for bank recapitalisation and 9 billion to Cyprus for a sovereign bailout and bank recapitalisation.

The Banking Union. There is widespread agreement that a successful banking union should encompass three elements: a single supervisory mechanism, a single resolution mechanism, and a common guarantee scheme for depositors. The first element, the supervisory mechanisms, was agreed to in 2013. It will be led by the ECB, and it is planned to be effectuated in autumn 2014. The initial idea was to subject all banks to a single supervisor; however, ultimately that scope was reduced to the supervision of only 130 “systemically important” banks. As to bank resolution, a conceptual agreement regarding the respective mechanism was achieved only in late December 2013. Bank resolution is of critical importance, yet it will take another year before the corresponding legal texts are finalised and will come into force (the finalisation of legal texts is planned for spring 2014). Despite the high stakes involved, and contrary to earlier expectations, the agreed resolution fund – a pot of money from which weak banks would be recapitalised or winded-down – will remain a national affair until 2026. Such a “solution” effectively undermines the whole idea of a banking union, because now the ECB, in its role as a supervisor, will have little incentive to put pressure on the weakest banks as this would undermine the public finances of struggling countries.⁵⁹ As a result, the European banking system will become more national than it has been since the inception of the euro. This also means that the credit crunch in banking sector will be prolonged, and there will be less credit available in the periphery of the eurozone for many years ahead.

the United Kingdom, and it entered into force on 1 January 2013 for the 16 states which completed ratification prior to this date.

⁵⁷ Wolfgang Münchau, An Exercise in Prolonging a Banking Credit Crunch, Financial Times, 22nd December, 2013.

⁵⁸ These are the European Financial Stabilisation Mechanism and the European Financial Stability Facility.

⁵⁹ The ECB proposal that during the interim period bank recapitalisation is financed from the ESM has also been rejected.

The economic union. An economic union denotes, basically, closer cooperation and joint decision-making in areas like taxation and labour and product markets. So far, the only noteworthy event has been proposals to establish (1) a rule of *ex ante* coordination of plans for major economic policy reforms, and (2) a convergence and competitiveness instrument which would consist of two parts: contractual arrangements for member states to undertake specific reforms and financial support to help member states implement these reforms. A blueprint of these proposals was considered by the European Council in December 2013. Except Germany, all other member states resisted this offer, and, therefore, the idea of contracts was postponed to the end of 2014. Some considerations as to why this happened include:

- 1) The neoliberal smack of the targeted reforms – namely, the deregulation of labour and product markets;⁶⁰
- 2) The associated assistance would be likely to take the form of loans or loan guarantees and not of grants;⁶¹
- 3) The main beneficiaries of assistance, admittedly, would be Italy and France (the other vulnerable eurozone countries are already undergoing similar reforms under their official bailout arrangements);
- 4) The “contracts” would be deeply unpopular, as the public could perceive them as a Brussels diktat. Besides, such proposals would carry a significant risk of moral hazard.

The conundrum of the politics of European economic integration. In summing up the achieved progress in the direction of creating a genuine economic and monetary union, one can detect several distinctive tendencies:

- European integration is being renationalised. Many newly introduced instruments (the European Stability Mechanism, the Fiscal Compact, the Competitiveness Compact) for closer integration are intergovernmental in nature, and the guardian of these is not the European Commission, but the German government;
- The role of the European Commission, most notably of its president, is being dissolved and, thus, seriously weakened. The choice of a weak personality for the president’s post, the simultaneous establishment of the posts of president of the European Council and of president of the Eurogroup are indicators of the dissolution of the powers of the European Commission;
- Proposals for new solidarity instruments like the mutualisation of debt, fiscal risk sharing and the common bank resolution fund are being consistently blocked. What is more, under the pretext of austerity, the already existing solidarity mechanisms like the EU budget are being downsized;
- The European social model is consistently being attacked. A phase of neoliberal and, one must say, authoritarian transformations has started. The only area where so far substantial progress has been achieved is fiscal discipline. In the meantime, little

⁶⁰ Steffen Stierle, “Convergence and Competitiveness Instrument.” Troika Watch, April 2013. Last accessed on 06.01.2014. <http://www.troikawatch.net/convergence-and-competitiveness-instrument/>

⁶¹ The battle for euro-zone reforms: Angela all alone. A blog on The Economist website, 20 December 2013. Last accessed on 06.01.2014. <http://www.economist.com/blogs/charlemagne/2013/12/battle-euro-zone-reforms>

concern has been expressed towards growth enhancement, equality and well-being. The solution to existing problems is being left to national discretion.

A thought-provoking theoretical framework to the existing fundamental problems of the EMU has been proposed by economic historian Kevin O'Rourke.⁶² By employing insights from two strands of literature – monetary integration and global governance – he concludes that the eurozone “occupies an uneasy half-way house in both economic and political governance” and “that there are no optimal policy solutions, only difficult trade-offs, with potential losers in each case”.⁶³

According to O'Rourke, the establishment of the EMU was a response to the economic trilemma (Mundell-Fleming) faced by the member states of the European Union (then Communities). The trilemma was that a country could pursue only two out of three targets simultaneously: monetary sovereignty, free capital movement and/or a fixed exchange rate. Under global pressure, the member states chose to give up their monetary sovereignty – otherwise it was not possible to ensure the smooth functioning of the internal market.

Yet the introduction of a single currency was a radical step from the perspective of another, political trilemma. This trilemma was discovered by Dani Rodrik and it contends that it is only possible to achieve two of these three things: national authority, global (European) integration and democracy (popular consent). In pursuit of these goals, one has to be sacrificed. The radicalism of the EMU was that monetary policy-making was not only abandoned, but delegated to a technocratic central bank. Moreover, this transfer of powers was not complete, as complementary areas like financial and banking regulation and fiscal policy were left within national competences. Yet the problem is that without these complementary areas, the working of the EMU has produced deep political cleavages between “core and periphery taxpayers” and also between “employed and unemployed” people.

The bitter conclusion of O'Rourke's analysis is that powerful interests are making it difficult to agree on further shared policies, be it banking or fiscal policy. National governments dominate national and EU policy making; therefore, according to the political trilemma, there are only two options: either integration proceeds (ignoring popular opinion), or the EMU project will fail. However, if the EMU fails, then, according to economic trilemma, member states will also have to abandon the single market.

A lack of strategic vision and a confidence crisis impedes the resolution of the eurozone's woes. The eurozone suffers from a lack of strategic vision – a vision that is workable for the whole eurozone. There are several observations that should be made in this regard:

First, as has been already mentioned, the sense of crisis has receded and with that also the momentum for change. In the middle of 2012, the European member states, including Germany, agreed that in order to save the single currency, deeper economic and political

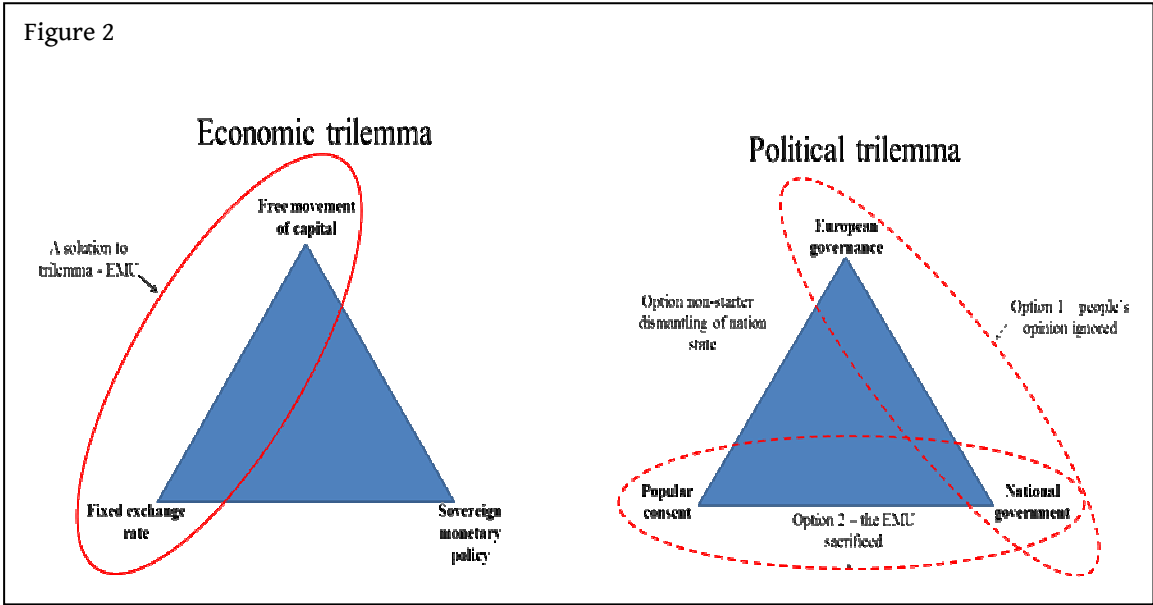
⁶² Kevin O'Rourke, A Tale of Two Trilemmas, March 2011, http://ineteconomics.org/sites/inet.civicaactions.net/files/BWpaper_OROURKE_040811.pdf

⁶³ Two trilemmas in Eurozone governance, Blog by niamh, 3rd May, 2011, <http://crookedtimber.org/2011/05/03/two-trilemmas-in-eurozone-governance/>

integration is indispensable. At the end of 2012, not long after the famous pledge of the ECB to buy the bonds of distressed eurozone member states, German Chancellor Angela Merkel announced that Germany had shown enough solidarity and that further integration should focus on enforcing economic discipline and competitiveness. Yet everybody knows that if the worst scenario happens and the eurozone collapses, Germany, as the eurozone’s greatest creditor, has the most to lose.

Second, it seems that the major problem is a huge mistrust which has developed between the eurozone’s major creditor country, Germany, and the debtor countries (Greece, Italy, Spain, Portugal, Ireland, and France). And, apparently, Germany also suspects that the European Commission has been captured by the interests of debtor countries. Germany has been a paymaster for the Union since the establishment of the Communities in the 1950s. True, Germany has also benefited a lot from the Union, but nonetheless, in Germany’s perception, the moment has arrived to change profoundly the way that the Union is run – otherwise it will cost too much for the country.

Third, Germany is in a good position to impose its will and it does not hesitate to exercise its clout. Germany alone commands one-third of the eurozone’s economy, and with the French and Italian economies in serious decline, Germany has become the unmatched leader of the eurozone. Yet there are two major problems with German leadership. One problem is related to its approach. At the moment, Germany, in a self-complacent manner, insists on copying its own ordoliberal macroeconomic model, focussed on export prowess through competitive wages and fiscal discipline. Other member states follow the German “diktat” out of desperation.⁶⁴ However, this is not the right approach for a *de facto* European hegemon. Germany is reluctant to accept this role, but nonetheless it will not be able to get away from that responsibility easily. Like the United States proposed the



⁶⁴ Wolfgang Münchau, An Exercise in Prolonging a Banking Credit Crunch.

Marshall Plan, which helped to shore up the ruined economy of West Germany, Germany now has the responsibility to propose a workable strategic plan for Europe, a plan that shows some degree of sympathy towards the problems of the southern regions.⁶⁵

The other problem is that Germany's economy is not as strong as it appears at first glance. While giving instructions to others, it has undertaken no growth-enhancing reforms at home in many years. The population is aging, and the push for green energy has left its people with power bills 40% higher than the EU average.⁶⁶ And it seems that the country's export dexterity is not an indicator of excellence and competitiveness, but, on contrary, is a sign of feeble domestic investment and consumption.⁶⁷ Germany and the whole Union would gain much from the deregulation of Germany's services sector and an upgrading of public infrastructure. Besides, Germany knows very well that structural reforms cost money. During its last reform phase in 2002, it broke the European fiscal rules itself.

Fourth, the eurozone, including Germany, will have to face the moment of truth sooner or later. Debt problems will not simply fade away, nor will the "zombie" banks. The debt-deflation spiral continues to spin and very likely will lead to other defaults, be it banks or sovereigns. Italy is not very far from catastrophe, and doubts are growing about France as well. Besides, the problems of weak growth and high unemployment erode support for the single currency, and the popularity of populist anti-European parties is on rise all over the European Union. The current saviour, the ECB, will not be able to play this role endlessly. There are limits to how far the ECB can go. So, the million dollar question is when the X hour will arrive, and how dramatic and costly the adjustment will be.

Conclusions – a way forward in 2014 and beyond

Despite the previous pessimism, there is still room for some optimism. The euro has brought considerable benefits to its users. It has also become the second most important currency in the world. As noticed by Kathleen R. McNamara, an American researcher, "the EU remains a remarkably solid and vital political structure nowhere near to the brink of collapse. The dramatic headlines mask the ongoing evolution of an extraordinary constitutional order that is more robust than any other interstate relationship".⁶⁸ The collapse of the eurozone would be extremely costly. The hope is that the instinct for survival will ultimately prevail and force member states to agree on a workable solution.

In Germany a new grand coalition government was formed at the end of 2013. The policy of Angela Merkel, the old-new chancellor of Germany, towards the rescue of the eurozone has been widely supported by the German public. People see her as a trustworthy custodian of German wealth against the dangers of the mutualisation of the public debts of profligate partners from the eurozone. Yet even Merkel has acknowledged the hidden costs of her policies. The Social Democratic party of Germany is now part of the new government. The social democrats have traditionally been more open-minded about greater European

⁶⁵ As reported by newspapers, the IMF has admitted a mistake in calculations of the effect of fiscal multiplier for Greece and Portugal (from 1 to 1.7), and that both countries should have had been given more time to reduce their deficits. See IMF Admits It Underestimated the Fiscal Multiplier, <http://www.eurointelligence.com/>

⁶⁶ Germany and Europe – the reluctant hegemon, *The Economist*, print edition, 15th June, 2013.

⁶⁷ Europe's economic rules – Brussels v Berlin, *The Economist*, print edition, 16th November, 2013.

⁶⁸ Kathleen R. McNamara, Can the Eurozone Be Saved?, *Foreign Affairs*, 7th April, 2011.

integration and solidarity. Hopefully, with their help the new government will change its stance towards the eurozone crisis and will raise German public awareness about the riskiness of the no-change policy to Germans themselves.

As to Latvia's policy makers, for them a period of hard work lies ahead. First, the internal reform agenda should be recalibrated in order to take into account the social and economic challenges that the Latvian public is facing: the quality of education, social care and healthcare, the effectiveness of the judicial system and competition policy, the existence of an industrial policy, creating a friendlier environment for grass-root entrepreneurs, etc. The interests of the people should be put forward, and that should be reflected in the structure of taxation.

Second, as far as European issues are concerned, the agenda should focus on the following issues:

- More ambitions towards restructuring the EMU framework – go back to the initial blue print;
- Support for a full banking union (2014 will be critical year);
- Support for greater centralisation of powers within the hands of European institutions (Latvia has more impact on the European Commission than the German government);
- Push for a more effective and better funded convergence and competitiveness instrument (Latvia's current economic success may prove to be a smokescreen to much more serious problems);
- Push for diaspora support and labour market reforms on the EU agenda (Latvians will not come home soon, and without them the system of Latvia's social safety network will not be sustainable).

Latvia's success within the eurozone will depend largely on the prudence and vigilance of Latvia's government.

CONDITIONS AFFECTING TACTICAL NUCLEAR WEAPONS IN EUROPE

*Imants Lieģis*⁶⁹

The use of chemical weapons in Syria last year once again showed the awful devastation that weapons of mass destruction can cause. It had echoes of the horrific scenes of Hiroshima and Nagasaki from 1945, when atomic bombs were used in the closing stages of World War II. This is why it is politically so important to work towards the prevention of the use of, and indeed elimination of, such weapons. However, the philosophical, moral and rational arguments in favour of nuclear disarmament face the enormous challenge of how to achieve the goal.

Looking back on the last two decades, the good news is that nuclear weapons bases in Latvia were closed down after the re-establishment of independence in 1991, and a series of combined unilateral-reciprocal measures have resulted in the U.S. and Russia retiring or destroying thousands of these weapon types previously meant for use in Europe.

However, on a global level the bad news is that during the same period the Asia region has seen Pakistan and India become nuclear powers, whilst there is an assumption that the DPRK and China have also increased their nuclear stockpiles.

Multilateral nuclear disarmament and non-proliferation are issues that cannot easily be separated from broader questions of defence and security. In examining specific issues relating to nuclear weapons that are of concern to Latvia as a NATO member, this essay will give some general background information on what are referred to as “tactical” (also referred to as “non - strategic”) nuclear weapons in Europe, touch on the broader security questions that encompass the discussion about the reduction of such weapons and consider what prospects there are for developments during 2014, bearing in mind the events of 2013.

⁶⁹ *Author's note:* I would like to acknowledge that I have benefited greatly in discovering more about nuclear disarmament and non-proliferation thanks to my involvement as a board member of the European Leadership Network (ELN), a non-partisan, non-profit organisation registered in the United Kingdom that works, amongst other things, to promote greater understanding about these issues. I am grateful to Latvia's ministry of foreign affairs for giving me the chance to continue my involvement with the ELN.

The views expressed in this article are entirely those of the author and do not necessarily reflect those of Latvia's ministry of foreign affairs or the ELN.

Overview

The presence of American tactical nuclear weapons on the territory of Europe was not only criticised by anti-nuclear groups during the Cold War, but also remains controversial today. For Latvia, the question of tactical nuclear weapons is the most important one when considering the general issue of nuclear weapons.

The dual-capable aircraft used for nuclear missions, together with an estimated 150-200 deployed U.S. B61 warheads, are assumed to be hosted by NATO members Belgium, Italy, Germany, the Netherlands and Turkey.⁷⁰

Whilst there have been calls for the removal of U.S. tactical weapons from Europe, in practice the joint position of NATO has determined the position of all member states, even though some see the weapons as having very little military value.⁷¹ On the other hand, it is perceived by others that there is a deterrence value in the presence of the weapons and that their continued deployment constitutes an important part of the U.S.'s commitment to its European allies.

In parallel with what is called the “U.S. nuclear umbrella” over Europe, there are also weapons held by two other UN Security Council and NATO members – France and the United Kingdom. Whilst these are important in themselves, for the purpose of this exposé I will confine myself to considering only U.S. tactical nuclear weapons.

The Dutch and Belgian governments back in 2010 joined Germany (together with Norway and Luxembourg) in calling for the removal of U.S. tactical nuclear weapons from Europe, but this question failed to unite allies when placed on the NATO agenda at the foreign ministers' meeting in Tallinn in April 2010. In particular, then State Secretary Hillary Clinton declared that “as long as nuclear weapons exist, NATO will remain a nuclear alliance”, a phrase that was subsequently placed in NATO's Strategic Concept at the Lisbon Summit in 2010. The Strategic Concept went on to stress that the nuclear forces of the Alliance provide the supreme guarantee of allies' security and contribute to deterrence.

A more detailed focus on the deterrence role of nuclear weapons was given by the NATO Deterrence and Defence Posture Review (DDPR), endorsed at the Chicago Summit in 2012. This maintained the status quo amongst the allies and upheld the important principle of “cohesion” amongst members by stating that “the nuclear force posture currently meets the criteria for an effective deterrence and defence posture”. It also mentioned creating “the conditions... for further reductions of non-strategic nuclear weapons assigned to NATO”.⁷²

Calls for the removal of U.S. tactical nuclear weapons from Europe sometimes appear to be louder than concerns about the estimated 2,000 Russian tactical nuclear weapons based in the European part of Russia and their role in Russia's military doctrine. During discussions on these issues in the past few years, I have on several occasions heard calls for the unilateral withdrawal of U.S. tactical nuclear weapons from Europe. This seems odd given the disparity of numbers – there are some 2,000 Russian weapons as opposed to 200 U.S.

⁷⁰ Tactical Nuclear Weapons and NATO (US Army War College Strategic Studies Institute), 259.

⁷¹ Ibid, 261.

⁷² Deterrence and Defence Posture Review, Press Release (2012) 063, 20.05.2012, NATO, http://www.nato.int/cps/en/natolive/official_texts_87597.htm?mode=pressrelease

ones. It therefore seems clear that, given the disparities, reductions should take place in a reciprocal and robustly verifiable manner.

Russia's position is also categorical – namely, that one of the preconditions for even starting discussions on the presence of these weapons in Europe is the complete withdrawal of U.S. weapons and the elimination of the infrastructure that could help to deploy these weapons on the continent.⁷³

There was a lot of hope that the U.S. administration under President Barack Obama would make greater progress in reducing tactical nuclear weapons following his speech in Prague in April 2009. Whilst the issue of strategic nuclear weapons has been addressed with some success, given the signing and ratification of the New Start Treaty by the USA and Russia, progress on the issue of tactical nuclear weapons has remained more elusive over the last five years. To have a fuller understanding of why this is so, it is necessary to look at wider considerations.

Broader security questions

As mentioned above, nuclear disarmament, or more specifically the reduction of tactical nuclear weapons in Europe, needs to be looked at in the context of defence and security in Europe as a whole. It is worth starting with the question of America's engagement in Europe through the "transatlantic link".

The U.S. Marshall Plan assistance to parts of post war Europe, coupled with the founding of NATO in 1949, were the linchpin of America's engagement in and commitment to Europe for the ensuing half century. Latvia, together with many other European countries in the eastern part of the European continent, were unable to benefit from this U.S. engagement. Although *de facto* occupied by the Soviet Union since 1940 (with an interruption by Nazi German occupation from 1941-1945), Latvia, Lithuania and Estonia were never acknowledged by the USA (and other Western countries) as being legally within the Soviet Union. This policy approach was of particular importance when the countries re-established independence in 1991.

When joining NATO 55 years after the Alliance was established, Latvia valued very highly the U.S. commitments to defence and security, especially concerning the core collective defence parts. Latvia became more secure than at any time in its history, which explains the sensitivities surrounding any diminution of collective defence, whether related to nuclear weapons or other aspects. Together with all countries that joined from 1999, Latvia also accepted the NATO "three no's" policy, namely that "NATO has no intention, no plan and no need to station nuclear weapons on the territory of any new members". This essentially meant that, alongside the other new member states, the four new NATO members with a border with Russia – Poland, Estonia, Latvia and Lithuania – became nuclear free territories within the Alliance. This informal NATO-Russia agreement was probably a concession given to Russia to help swallow the bitter pill of NATO enlargement.

The post 9/11 rifts between some European states and their U.S. ally were followed by louder and more recent American concerns about the lack of financial commitment to

⁷³ Alexander S.Kolbin: Russia and NSNW Reductions: Separating the Wheat from the Chaff, Working Paper, The Warsaw Workshop, 7-8 February 2012.

defence spending amongst a majority of European NATO allies. Although the rifts that have arisen over the last decade or so have often appeared fundamental, it seems unlikely that America would disengage from Europe and essentially abandon NATO and the transatlantic link. This does not mean that Europe should remain complacent about America's ongoing commitments.

Set against justified U.S. concerns about Europe not pulling its weight financially – America now provides about 75% of NATO's defence budget – are concerns expressed by some Europeans about the downsizing of U.S. troops in Europe and America's apparent turn away from Europe with its so-called "pivot" towards the Asia Pacific region.

Over the past few years America has downsized the number of brigades present in Europe and withdrawn military hardware. The concept of a U.S. Ballistic Missile Defence of Europe has also undergone adjustments during recent years, and about one year ago the USA announced that the planned fourth phase of its European Phased Adaptive approach would be abandoned. Following a tentative agreement with Iran concerning its nuclear programme, Russia has suggested that NATO's Missile Defence system, incorporating the U.S. system, is no longer of relevance. The combination of these events have occasionally led to concerns being expressed about the U.S. commitment to Europe.

Such concerns have been exacerbated by, amongst other things, the Pentagon announcement in January 2012 that "while the U.S. military will continue to contribute to security globally, we will of necessity rebalance toward the Asia-Pacific region".⁷⁴ Although this has led to the deployment of U.S. marines to Australia, there have also been suggestions made that in fact the pivot has failed to materialise in any significant way and indeed that U.S. influence in the region is receding.

So whilst the U.S. remains the world's strongest military power, it seems that there are concerns in various regions about the waning of U.S. engagement or interest. Voices of concern are heard not only in Europe, but also elsewhere. At the same time, 2013 brought some positive signs for Northern Europe (and hence Latvia), which even led Estonian President Toomas Hendrik Ilves to refer, albeit jokingly, to a U.S. "pivot to the north"⁷⁵ of Europe. This comment came on the heels of news about two particular events: namely, the meeting of Obama with the three presidents of Estonia, Latvia and Lithuania in Washington on August 30th and President Obama's subsequent visit to Sweden and meeting with the Nordic heads of government in Stockholm in September.

For Latvia and other countries on the periphery of NATO, the U.S. presence in and commitment to Europe are of paramount importance to security. Hence, the assurances given publicly to the Baltic presidents when they were in Washington concerning the U.S.'s commitment to NATO and the soundness of the collective defence commitment were significant. To quote Vice President Joe Biden's comments published at the time of the visit, "President Obama and I consider Article 5 of the NATO Treaty to be a solemn obligation for the United States – not just for our time, but for all time."⁷⁶

⁷⁴ United States of America Department of Defence, Sustaining U.S. Global Leadership: Priorities for 21st Century Defence, January 2012, http://www.defense.gov/news/Defense_Strategic_Guidance.pdf

⁷⁵ Tweet @ Ilves Toomas, 07.08.2013.

⁷⁶ Latvijas Avīze, 30th August 2013.

The exposure by Edward Snowden of the U.S.'s surveillance of its European allies placed additional strain on the transatlantic link during 2013. However, the fact that negotiations on the EU-USA Transatlantic Trade and Investment Partnership (TTIP) Agreement went ahead in spite of the damage caused in Europe by the NSA surveillance scandal was a welcome outcome. These ongoing negotiations and the eventual signing of an agreement will also help with holding together the strategic transatlantic link.

So although Europe and NATO allies are still partners of first resort for America, fighting in Iraq and Afghanistan has taken its toll on a war-weary U.S. public that also appears increasingly inward-looking during President Obama's second term. It has also meant that, in cooperation with European allies, the U.S. has tried to develop a policy of "leading from behind" and decrease the burden on America in situations where Alliance defence and security concerns arise.

Given that decisions about reducing tactical nuclear weapons in Europe are primarily to be taken by Russia and the USA, it is important to also look at some aspects of U.S.-Russia relations, as well as certain developments within Russia itself.

Obama's decision to cancel the planned bi-lateral meeting with President Vladimir Putin at the G20 meeting in St. Petersburg was an indicator of the low point reached in bilateral U.S.-Russian relations. It also reflected how the U.S.-Russia "reset" had failed to produce the desired results. The "Snowden effect" clearly impacted U.S.-Russian relations, just as it had implications for U.S. relations with Europe. The twists and turns concerning reactions to the use of chemical weapons in Syria – whether or not to use military intervention, the involvement of the UN and Russia's deft manoeuvres in finding a solution – also showed how rapidly events can change the dynamics of bilateral relations between these two UN Security Council members. Getting Syria's leadership to acknowledge the possession of chemical weapons and accept steps towards the destruction of its chemical weapons stockpile perhaps enabled President Putin to offer the chance for other aspects of Russia's relations with America to be improved.

Despite various setbacks in their relations, it is important to recall that the USA and Russia have concluded the New Start Treaty on further reducing strategic nuclear weapons. There have also been some other small encouraging recent developments. At the G8 Summit in Dublin, a U.S.-Russian bilateral framework on threat reduction was signed. During his visit to Berlin soon thereafter, President Obama said that the U.S. will "work with our NATO allies to seek bold reductions in U.S. and Russian tactical weapons in Europe".⁷⁷ Of course as one of those NATO allies, Latvia will also have the opportunity to express its views on these questions to its U.S. partner. In that context, issues such as reciprocity and transparency in the process of reductions, and the importance of confidence building measures in cooperation with Russia, would probably be the issues that Latvia would be highlighting.

Whilst keeping an eye on the U.S.-Russia relationship, Latvia, as a NATO member that is also a neighbour of Russia, clearly closely follows defence and security developments within Russia itself. Despite the challenges, all avenues for continuing dialogue with Russia

⁷⁷ Remarks by President Obama at the Brandenburg Gate – Berlin, Germany, Pariser Platz, Brandenburg Gate, 19.06.2013., <http://www.whitehouse.gov/the-press-office/2013/06/19/remarks-president-obama-brandenburg-gate-berlin-germany>

need to be pursued. On the bilateral level, the Latvian foreign minister's trip to Moscow and meeting with his Russian counterpart in November was a positive development.

NATO has been unable to agree in discussions with Russia on the development of a missile defence architecture to protect both NATO and Russia. As NATO Deputy Secretary General Alexander Vershbow points out, "NATO's Ballistic Missile Defence system cannot pose any threat to Russia's strategic deterrent forces".⁷⁸ Despite positive cooperation in some areas between NATO and Russia (e.g., the transit of goods through Russia to and from the ISAF operation in Afghanistan), discussions on wider strategic issues have been hindered by a lack of agreement on missile defence.

Russia's confirmation in December of last year about deploying nuclear-capable Iskander missiles in the exclave region of Kaliningrad and elsewhere near to NATO's border⁷⁹ as a countermeasure to NATO's Missile Defence system was criticised by both NATO and the U.S. state department, as well as causing concern in the neighbouring Baltic countries and Poland. Statements about this issue were made by Latvia's prime minister and defence minister, with the latter questioning "...how we can increase our trust in Russia if they place these type of weapons by our border".⁸⁰

In spite of such actions running against the grain of the search for confidence building measures, it is imperative that this search continues to be pursued.

Regrettably, Russia's considerable increase to its defence budget, the holding of large joint military exercises together with Belarus close to NATO's western border (including a scenario using nuclear weapons in 2009) and its reliance on tactical nuclear weapons to cover for weaknesses in conventional forces make the search for confidence and trust building even more challenging.

Although regional organisations such as NATO and the Organisation for Security and Cooperation in Europe also offer opportunities for dialogue with Russia, their success has been very limited. That is why it is so important for other actors, such as NGOs and think tanks, to create alternative platforms for discussion. The work of organisations such as the Nuclear Threat Initiative, the Carnegie Endowment and the European Leadership Network is crucial in driving dialogue and trying to address core security issues so as to build up trust. Poland's increasing role as a significant regional security actor should also be noted, especially with the Polish Institute of International Affairs in Warsaw playing an active role in discussions relating to nuclear issues.

Prospects for 2014

The year 2014 will mark the first decade of Latvia's institutional return to the Euro-Atlantic fold. Together with various other countries that were consigned to the Soviet sphere of influence after World War II, Latvia joined NATO and the EU in 2004. Interestingly, Latvia joining the eurozone on 1 January 2014 has also been viewed from the security perspective, with references being made to the importance of greater integration into European

⁷⁸ Moscow Times, 13th November 2013.

⁷⁹ RIA Novosti and RT, Russia Confirms Deployment of Iskander Missiles on NATO Borders, 16.12.2013, <http://www.atlanticcouncil.org/en/blogs/natosource/russia-confirms-deployment-of-iskander-missiles-on-nato-borders>

⁸⁰ LETA, 17th December 2013.

structures as a way of staving off this type of political pressure from Russia, as was recently experienced by Ukraine.

On the broader question of the strategic importance of the transatlantic link, the two defining events during this year are likely to be the NATO Summit in September and the ongoing EU-U.S. negotiations on the TTIP.

The close of 2013 saw an EU Summit addressing defence and security issues and a new coalition government taking over in Germany under the continuing leadership of Angela Merkel. Neither of these two important events indicated that the question of nuclear weapons in Europe will be placed high on the security policy agenda in the foreseeable future. As far as Germany is concerned, the replacement of the Liberals by the Socialists as the junior coalition partner will appear to make little difference given that the liberal foreign minister's concerns about U.S. nuclear weapons in Germany expressed during the early days of the last coalition failed to make a subsequent impact on policy decisions.

Bearing in mind the current NATO nuclear position, as expressed in the 2010 Strategic Concept and the subsequent DDRP adopted at the Chicago Summit, it seems unlikely that there will be progress on these questions at this year's NATO Summit in the UK. The DDRP refers to creating "the conditions... for further reductions of non-strategic nuclear weapons assigned to NATO".⁸¹ "Creating the conditions" is the challenge, but factors such as an absence of willingness to engage on the part of Russia, together with the ongoing need to maintain Alliance cohesion, weigh against significant progress being made.

Which makes it all the more important to continue to pursue broader areas of discussion with Russia in forums outside these organisational structures. Such informal discussions, however, will always face the challenge of how to impact governments and get the nuclear issue onto their agenda.

Despite the challenges for any small country facing limited resources and competing priorities, let me offer some suggestions about how Latvia can contribute to the ongoing debates.

As a member of NATO and the EU for 10 years, Latvia has already gained unique insights into the working of both organisations. This provides the opportunity to continue to try to exert influence on decision making from the inside.

Latvia's history and geographic location are assets. This is especially true when we look at the highly developed nature of cooperation with neighbouring Estonia and Lithuania, which extends into cooperation with Nordic partners. Given Poland's size and strategic importance, this country is also a vital regional partner with whom Latvia will no doubt continue to strengthen relations.

As one of four recent EU and NATO member states bordering Russia, Latvia's specific expertise about this crucial neighbour is clearly something from which many other members within these two organisations will continue to benefit.

Latvia's reputation internationally has grown over the last few years thanks to the sound policies that led the country out of a financial crisis and culminated in recently joining the eurozone. Latvia can continue to build on and take advantage of these positive

⁸¹ Deterrence and Defence Posture Review, 20.05.2012, <http://www.nato.int/>

perceptions, especially with the leading EU country, Germany. At the same time, the approaching presidency of the EU Council in 2015 will also provide unique opportunities to influence, albeit within limits, some of the policy issues outlined above.

For a variety of reasons, the issue of nuclear weapons is not high on Latvia's foreign policy agenda. It rarely figures in public, academic or policy discussions on foreign policy. Which means that there are clearly opportunities available for raising awareness about these questions and addressing them by drawing on the existing regional and global expertise.

REFLECTIONS ON LATVIA'S DEFENCE POLICY IN 2013. THE WAY AHEAD AND CHALLENGES IN 2014

Raimonds Rublovskis

The year 2013 has been rather challenging for the Latvian Ministry of Defence (MOD) and, subsequently, for the Latvian National Armed Forces (LNAF). Despite several signs of recovery in the Latvian economy and financial system, the overall situation in the defence realm remained rather complicated and complex. The MOD had several main issues to handle in order to prevent a further decline of personnel quality and the military capabilities of LNAF.

Firstly, it was a permanent struggle for the MOD on the government level to raise the political will to sustain and increase the defence budget of the Republic of Latvia, in both the percentage of GDP and real money investment into the defence system of the country, ensuring a slow recovery from the financial crisis of 2008 that caused severe consequences for the LNAF. Secondly, the personnel issue was high on the agenda of the MOD in 2013. There were attempts made by the MOD to deal with challenges for the personnel policy of the LNAF, which included the task to ensure the recruitment of a sufficient number of personnel and further attempts to maintain the current number of personnel within the LNAF. Thirdly, it was necessary to sustain and maintain the operational readiness of the LNAF in order to fulfil the obligations of the Republic of Latvia concerning participation in international military operations abroad and scheduled military exercises on Latvian territory.

On the one hand, Latvia had entered 2013 with a set of renewed overarching documents on state defence issues, which were approved by parliament and the government in 2012, and those documents set the prospective of the perceived development of the Latvian defence system in the medium- and long-term. The New State Defence Concept of the Republic of Latvia was adopted by parliament, the government of the Republic of Latvia signed a commitment to reach 2% of GDP allocated to state defence by 2020, and the Long-Term Development Plan of the LNAF up to 2024 was approved by the government in 2012. However, one could argue that the implementation of all those concepts and plans has faced substantial challenges from the very beginning in 2013 due to the situation with the defence budget in terms of both the percentage of GDP allocated to state defence needs and real money investment, which are far beyond the timetable set by parliament, the government and the MOD to reach 2% of GDP for defence in 2020. The first and utmost challenge is that of the defence budget of the Republic of Latvia and the prolonged inability

of the MOD to display relevant arguments in order to improve the situation. Certainly the current situation in the country requires that the government significantly improve the situation in the economy, education, health care, demographics, and other urgent issues; therefore, the realm of defence seems to be rather low in the government's priority list. Latvia has received sustained criticism concerning the state of its defence budget and military capabilities from the NATO Alliance and a number of particular allies. One could argue that the argumentation of the leadership of the MOD to convince the government and general public to allocate more resources to the realm of state defence was insufficient, and Latvia still remains as one of the militarily weakest countries of the NATO Alliance in terms of political readiness to increase the percentage of GDP for state defence needs and real money investment for further technological development of the LNAF. Therefore, one could argue that the current pace of events concerning the defence system of Latvia will have a negative impact on the development goals which were set by the parliament and government in the State Defence Concept, the Long-Term Development Plan of the LNAF, and other commitments of the Latvian political leadership.

In 2013, the personnel issue remained high on the agenda of the MOD. Bearing in mind that significant numbers of highly professional and motivated personnel of all ranks retired in the 2008-2012 timeframe due to severe cuts to personnel costs in the defence budget, one could argue that the current quality of personnel in the LNAF has suffered a decrease of professionalism, motivation and vision. Moreover, taking into account demographic challenges that Latvia was still facing in 2013 and the high ratio of emigration, it is highly unlikely that the LNAF would be able to recruit and maintain sufficient numbers of educated and motivated personnel. One could argue that overarching documents of state defence display negative trends concerning the number of personnel of the LNAF. The previous State Defence Concept of 2008 stated that the limit on the LNAF is 5,800 military personnel, whereas the current State Defence Concept of 2012 lowered the number of military personnel to 5,500. However, the actual number of professional military personnel in the LNAF in 2013 was well below even the 5,000 benchmark, numbering slightly above 4,000 professional military personnel. This means that in 2013 the number of LNAF personnel was significantly insufficient when compared with the limits which were given in the current State Defence Concept. Therefore, one could foresee a significant challenge to fulfil the LNAF personnel development goals in order to reach the 6,000 personnel benchmark in 2024 as stated in the LNAF Long-Term Development Plan. Despite the previously mentioned challenges, one could argue that the Latvian military are well prepared and well equipped at the individual level – however, a lack of resources to significantly increase salaries and packages of social benefits for military personnel can and will negatively impact personnel development in the LNAF.

Another significant issue in 2013 remained the operational capability of the LNAF to participate in international military operations and scheduled military exercises on Latvian territory. As a small country with very limited resources that could be allocated to state defence needs, Latvia is heavily influenced by global and regional security and defence developments. Firstly, this applies to the situation within the realm of NATO-led international military operations. Secondly, as a border country of NATO and the EU, Latvia is influenced by developments in the Russian military, and subsequently, Russian military exercises. In 2013, Latvia participated in international military operations, and

Afghanistan was still the main effort of the LNAF internationally. However, as NATO is preparing itself to disengage from Afghanistan, that means that 2013 was the very last year for the LNAF to participate in this operation. Certainly, military personnel of the LNAF have gained significant military experience in international military operations within the last 20 years, and 2013 has been very important in consolidating that military experience.

The decision to create and develop a NATO Centre of Excellence (COE) for strategic communications in Latvia, certainly, was one of the very important decisions for Latvian security and defence policy within the network of NATO COEs. From the perspective of being marked on NATO's map of COEs, it could be viewed as a logical strategic decision for both NATO and the Republic of Latvia; however, the Latvian side would face several challenges in order to implement this project due to the financial restrictions of the current defence budget, as well as the intellectual capacity from Latvian side to cover such an important and strategic-level issue like strategic communications. One could foresee that the abovementioned issues would challenge the ability of Latvia to successfully implement this project in 2014.

From an operational perspective, 2013 was extremely important because of scheduled large-scale live military exercises in the Baltic area which were conducted by both NATO and the Russian Federation.

Zapad 2013 was a scheduled live military exercise which was conducted in September-October of 2013 by the Russian Federation and Belarus in the Baltic region. Previous exercises – Zapad 2009 and Ladoga 2009 – saw over 30,000 Russian and Belarusian military personnel engaged in the exercises. Therefore, Zapad 2013 could be viewed as a routine, although large scale, live military exercise. The point of view of the Latvian MOD concerning Zapad 2013 and their analysis of the set of events between Zapad 2009 and Zapad 2013 led to a statement from the MOD that both exercises had an aggressive stance against NATO in the Baltic region, and particularly against Latvia and the other Baltic States, in order to simulate a military assault against the Baltic States. The Latvian MOD saw this military exercise and previous events in the region as an attempt of the Russian Federation to increase its military presence in the Baltic region in the land, maritime and air domains. On the other hand, the official explanation of the Russian side claimed that the exercise, which encompassed 12,000 Russian and Belarusian military personnel, took a purely defensive approach and it had no plans for offensive operations against any NATO member in the Baltic region. One has to bear in mind the overall context of the global and regional security environment in 2013 to explain the situation surrounding the Russian military exercise Zapad 2013. Firstly, Latvia and the other Baltic States as members of the NATO Alliance enjoy the highest security level ever in their history, and the provisions of Article 5 are as solid as ever before. Secondly, the status of the relationship between Russia and NATO, as well as the bilateral relationship between Russia and the United States, has a profound impact on security and stability in the Baltic Sea region. However, taking into account the current global security environment, it is especially important for Latvia, and the Latvian MOD, to know and understand where the Baltic States stand within the priority list of security challenges for both the Russian Federation and the United States. One could argue that there has been a significant shift within the global security environment due to the fact that there are much more urgent issues and important regions for global security than Europe and, subsequently, the Baltic region.

The situation in Afghanistan beyond 2014, further developments in the Arab world, a rising China, and Iran's nuclear programme are only few global security issues which will dominate the global and regional security agenda in the years to come. The United States has already responded to these emerging security challenges with its Pacific Pivot strategy. It is certain that all abovementioned security challenges will also be high also on Russia's security and defence agenda; therefore, one could argue that Europe and the Baltic region is not a security concern for Russia, and as such is not high on the Russian security agenda for the time being because of different and more urgent challenges for Russia's security elsewhere. Therefore, one could conclude that Europe and the Baltic States remained relatively low within the security agenda of both the United States and the Russian Federation in 2013 – however, by conducting the large scale live military exercise Zapad 2013 in the Baltic region, Russia sent a clear political and diplomatic signal that although the country's strategic security challenges lies elsewhere on the globe, the Baltic region still remains strategically important for Russia because of historical and geographical reasons due to its proximity to the core territories of the Russian Federation.

Another important live exercise – Steadfast Jazz 2013 – was conducted by NATO in the Baltic region in November of 2013. The aim and scope of this NATO exercise was planned as the culmination of NATO Response Force (NRF) training in 2013. The event involved approximately 6,000 NATO military personnel, with 3,000 to participate in the live military exercise and an additional 3,000 to perform various headquarters duties, including command and control. Air, maritime, and land special operations components were involved in the planning and execution of the exercise, and the overall command and control arrangements were the responsibility of NATO Joint Force Command Brunssum (JFC) headquarters, which will lead any NATO joint operations in 2014. The aim of the NATO exercise was to train and test the NATO Response Force, which is a high readiness, technologically advanced multinational joint force which includes land, maritime, air and special operations components. The NRF must be able to respond to the full spectrum of potential military missions, including high-intensity combat missions. Therefore, the core purpose of exercise Steadfast Jazz 2013 was designed to test both live forces and the personnel of various headquarters in order to exercise command and control duties over NRF troops. Certainly, the Steadfast Jazz 2013 exercise was scheduled well in advance, and therefore both the Russian Federation and NATO had conducted rather large scale military exercises in close proximity to each other, as well as within a rather close time schedule. One could argue that Steadfast Jazz 2013 was mostly a politically determined event in order to send several political and diplomatic messages. Firstly, it was an internal message for NATO countries that the NRF effort is in place and ready to be used when needed; secondly, it was a message to the Baltic States to reassure them of the validity of NATO commitments towards all members of the Alliance; and thirdly, it was a kind of political response to the previous military exercise of the Russian Federation, Zapad 2013. However, one could argue that several trends proved that this exercise was mostly politically driven. Firstly, the United States – the core contributor to NATO in terms of budget and military capabilities – participated with a rather low profile, sending only a few hundred military personnel to take part in Steadfast Jazz 2013. Secondly, the total number of military personnel participating in the exercise was significantly lower than the number of Russian and Belarusian personnel that participated in the military exercise Zapad 2013. One could

argue that those facts are a message from the United States to the Russian Federation indicating that the situation within the global and regional security environment requires American military capabilities to be deployed in much more important regions, and clearly showing that Europe and, subsequently, the Baltic region is not considered by Americans as potentially dangerous from the security and defence perspective. However, from NATO's perspective it was necessary to send a political signal to the political leadership of the Baltic States to assure them of the commitment of the Alliance towards the Baltic States. The visit of NATO Secretary General Anders Fogh Rasmussen to Latvia during the exercise and his meeting with the presidents of the three Baltic States was the political message from NATO leadership to the Baltic States.

Finally, one can draw some conclusions regarding the impact of the year 2013 on the Latvian defence sector and possible trends and challenges in 2014. Firstly, the consequences of the global financial crisis have been very severe for the economy of Latvia and, subsequently, for the defence budget of the Latvian MOD, which has suffered significant cuts since 2008. Although the overall situation in 2013 has slightly improved, however, the defence budget of the Republic of Latvia in 2013 is not even close to the figures of Latvian defence spending in 2007, in terms of both percentage of GDP and in real money investment. Therefore, one could conclude that the defence system of Latvia has started a slow recovery in 2013. Although the necessary overarching documents within national defence realm had been approved by parliament and the government, the current pace of increase of the defence budget is too slow to achieve the development goals of the LNAF in the medium and long-term perspectives; subsequently, 2013 has not made a significant breakthrough and the target figures of 2% of GDP allocated to state defence needs by 2020 and the LNAF development goals by 2024 most probably will not be met.

The most important challenges for the recovery and development of the LNAF in 2014 will be related to the political processes in Latvia and abroad. The elections of EU Parliament, the national elections of the parliament of the Republic of Latvia in October of 2014, and the upcoming NATO Summit in the United Kingdom will certainly have deep impact on the defence realm of the country. One could argue that issues of demography, economy, education and other social aspects will be high on the pre-election agenda of any of political parties; therefore, one would expect that state defence issues will be marginalised in 2014. The situation is even more complicated in 2014 due to the resignation of the government of Valdis Dombrovskis, heated political consultations in order to forge a new government of the Republic of Latvia, and the introduction of the euro currency. From an international perspective, the upcoming NATO Summit which will be held in Cardiff, Wales, will also be extremely important for the future of the security and defence policy of the Republic of Latvia. Firstly, current NATO Secretary General Anders Fogh Rasmussen will leave his office; therefore, the member states of the Alliance have to decide who will be the next NATO Secretary General. For small nations, including Latvia, the personality of the leader of the Alliance matters much more than for more powerful members of NATO. Secondly, generally speaking NATO is in rather bad shape due the fact that several leading states of the Alliance are engaged in different urgent issues, leaving defence matters marginalised. The United States with its Pacific Pivot strategy considers NATO increasingly irrelevant for American security due to the continuous inability of European members of NATO to fulfil their obligations within the defence realm. The United Kingdom might be

more interested in the 2015 British General election than the immediate future of the Alliance, and France had made decisions to intervene militarily in Mali and the Central African Republic without reliance on NATO or EU military support. Germany has its own challenges in domestic and foreign policy. From the Latvian perspective, the positions of main actors of the Alliance definitely display a lack of coherence in NATO for the time being, and this is an alarming signal for Latvia. One could conclude that decisions which will be made in the next NATO Summit will be very important to the Republic of Latvia.

All the previously mentioned aspects will put substantial pressure on the defence realm of the country. Firstly, state defence issues will not be high in political life in 2014; most probably, state defence issues will not be instrumental in pre-election discourse among the political parties in 2014. Secondly, although the defence budget in 2014 has slightly increased, it is still more than insufficient to cover the operational, personnel and development goals of the LNAF, and in a pre-election atmosphere it is not likely that there will be the option to increase the defence budget in 2014, or plan significant improvements for 2015.

Taking into account the previously mentioned arguments, 2014 will be a rather difficult year for the Latvian MOD. The State Defence Concept, the LNAF Long-Term Development Plan and the government's commitment to increase defence spending to 2% of GDP by 2020 are all overarching documents that require a certain road map in order to achieve the approved goals. However, one could argue that 2014 will be difficult in terms of sustaining the necessary pace to reach the development goals of the MOD and LNAF in due time. Moreover, although the defence budget of 2014 cannot be considered as a development budget, LNAF personnel issues and operational issues are increasingly important. The MOD and LNAF still have to find the resources to sustain and maintain professional military personnel within the system, adjusting salaries and social benefit packages for military personnel in order to avoid the early retirement of qualified military personnel in 2014. From an operational perspective, although scheduled military exercises will be conducted in Latvia in 2014, the most important issue is that the Latvian military will leave Afghanistan in 2014, and with it a substantial participation in international military operations will be terminated. This fact will also bring additional challenges to the MOD and LNAF because military personnel will lose additional income, combat experience and interoperability with other militaries. One could foresee 2014 as a rather difficult and challenging year for Latvian defence sector.

THE EASTERN PARTNERSHIP: LESSONS LEARNED FROM THE VILNIUS SUMMIT AND THE WAY AHEAD TO THE RIGA SUMMIT

Mārtiņš Vargulis

The Eastern Partnership (EaP) was set as one of Latvia's main foreign policy priorities in 2013. The EaP and Central Asia in Latvia's foreign policy priorities for 2013 were defined "as the most promising directions".⁸² From the perspective of the ministry of foreign affairs of the Republic of Latvia, a) these countries highly appreciate Latvia's reform efforts and, in their aspirations to strengthen relations with the European Union, see Latvia as a natural partner, b) Latvia is well acquainted with those regions and since the restoration of independence has established an active economic and political dialogue with the regions' countries.⁸³ These preconditions have encouraged representatives of Latvia's Foreign Service to enhance the intensity of relations with EaP countries. In 2013, Latvia was a strong supporter of the EaP initiative and continued to officially declare its willingness and determination to support EaP countries' efforts to strengthen relations with the EU. An important role has been already given to the EaP in the context of the Latvian Presidency of the Council of the European Union. During 2013, however, EU leaders faced several challenges in this neighbourhood.

The initiative, which originally was conceived as a simple "win-win" policy for both EaP countries and the EU, soon proved to be a very complicated task for EU leaders. The previous year has contained a number of signs of this: a) each partner country requires a specific bilateral EU approach, b) diverging domestic political developments, as well as different foreign policy directions and business climates in the EaP countries, are factors that hindered the EU from applying "one-size-fits-all" policies to all its partner countries, c) the EU itself has, at times, lacked internal unity, which has resulted in contradictory signals to EaP partners and other international actors. Emerging challenges have forced EU leaders, and Latvia as a part of it, to overlook the EaP initiative, which has been implemented since 2009. The opportunities and challenges that the EU and Latvia itself faced during the previous year give the possibility to evaluate its policy towards the EaP

⁸² Foreign policy priorities for 2013 – preparation for EU Presidency and support to euro adoption, 24.01.2013, Ministry of Foreign Affairs of the Republic of Latvia, <http://www.mfa.gov.lv/en/news/press-releases/2013/january/24-2/>

⁸³ Ibid.

and indicate the main tasks for the upcoming Latvian Presidency of the Council of the European Union and the Riga Summit in 2015, for which preparation work will mainly take place in 2014.

Therefore, this chapter is structured as follows. Firstly, Latvia's bilateral relations with EaP countries are reviewed and its policy towards the EaP assessed. Secondly, the overall context of the EaP is discussed, assessing EU policy towards EaP countries. Thirdly, some challenges are defined in terms of the Riga summit. Finally, some recommendations are offered for the year 2014 and beyond.

Latvia's policy towards Eastern Partnership countries

According to the ministry of foreign affairs of the Republic of Latvia, the main priorities of Latvia in the context of the Eastern Partnership during the Lithuanian Presidency of the Council of the European Union were as follows:

- 1) Continue supporting the process of political rapprochement and economic integration with the EU by the Eastern Partnership countries;
- 2) Stand up for achieving significant results at the Eastern Partnership Summit to be held in Vilnius on 28 and 29 November 2013;
- 3) Give direct attention to the issue of signing the Association Agreement with Ukraine and initialling agreements with Moldova, Georgia and Armenia, as well as take further action towards visa policy liberalisation;
- 4) Stimulate discussion on the development of the Eastern Partnership in the wake of the Vilnius Summit;
- 5) Support efforts to improve EU-Belarus relations.⁸⁴

In 2013, Latvia took active part in all five abovementioned directions/priorities. Obviously, some of these have been more successful than others. Some of them Latvia itself could not influence to a large extent. Nevertheless, looking back at 2013, Latvia's foreign policy was focussed on supporting the process of political rapprochement and economic integration with the EU by the Eastern Partnership countries. This is proved by Latvia's foreign policy calendar, which was enriched with various bilateral and multilateral meetings with high representatives from all EaP countries. Latvia in various formats of meetings with its EaP counterparts has expressed its commitment to contribute to the future of the EU's neighbourhood policy in order to promote support for the political and economic development of the Eastern Partnership countries.

In 2013, probably the least active cooperation among EaP countries that Latvia experienced and implemented was with regards to Armenia. The most significant event in bilateral relations between Latvia and Armenia was the appointment of well-known and experienced Ambassador of Latvia Elita Gavele to the Republic of Armenia. In her accreditation address, Latvia's Ambassador noted the importance of the Eastern Partnership, whilst expressing hope that Armenia will continue on its course towards

⁸⁴ Priorities of Latvia During the Lithuanian Presidency of the Council of the European Union Second Half of 2013, Latvian MFA, <http://www.mfa.gov.lv/en/eu/Presidencies/lithuanian-presidency/>

European values.⁸⁵ However, compared with other EaP countries Armenia seems a less important partner to Latvia. Even after Armenian President Serzh Sargsyan expressed his plan for Armenia to join the Russia-led Customs Union, no official statement by the ministry of foreign affairs of the Republic of Latvia was announced. Although Armenia over the last two years was regarded as a champion of the negotiation process among EaP countries, the u-turn of Armenia's president was not a complete surprise to EU leaders or to Latvian authorities. For many years Armenia had tried to balance between three chairs – the USA, Russia and the EU. The possibility was not unheard of in the corridors of the ministry of foreign affairs of the Republic of Latvia that the intensified geopolitical competition that was taking place in the region would make Armenian leadership choose the chair with “Russia” inscribed on it.

An active role in Latvia's foreign policy towards Central Asia was played by Latvian President Andris Bērziņš, who made several working visits to the republics of this region. In April 2013, a Latvian delegation including the foreign minister and president of the Republic of Latvia made a working visit to Azerbaijan. Both Latvian and Azerbaijani representatives acknowledged that President Andris Bērziņš's official visit to Azerbaijan had added a fresh impetus to strengthening relations and setting up successful contacts between entrepreneurs from both countries.⁸⁶ According to the Investment and Development Agency of Latvia, economic cooperation between Latvia and Azerbaijan during recent years has significantly increased. Although Azerbaijan in 2012 was only the 41st biggest export partner and 65th biggest import partner for Latvia,⁸⁷ there are ambitions and plans for Latvian entrepreneurs to increase their business ties with Azerbaijan. Last but not least, Latvian representatives positively evaluated the signing of the EU-Azerbaijan Visa Facilitation and Readmission Agreements,⁸⁸ which can lead to the promotion of people-to-people contacts between Latvians and Azerbaijanis.

Visa liberalisation is an aspect of the utmost importance for EU's ability to attract EaP countries. Visa liberalisation guarantees not only easier travelling but also facilitates business and working visits. It gives more possibilities to students to participate in various youth projects that are taking place in EU. However, the EU should take notice of the risk factor in the context of the implementation of a free visa regime with EaP countries. Without structural reforms in the judiciary, rule of law and eradication of corruption fields, a free visa regime could lead to the migration of educated people to EU. Therefore, visa issues cannot be excluded from the overall assessment of a particular EaP country's economic and democratic situation.

Compared to Armenia and Azerbaijan, more focussed and comprehensive cooperation was implemented with regards to Georgia and Moldova. Latvia actively supported Georgia's and Moldova's willingness and readiness to initiate Association Agreements with the EU. For instance, in order to support the progress achieved by Moldova in the EU-related reform

⁸⁵ Ambassador of Latvia Elita Gavele Accredited to Republic of Armenia, 13.12.2013, Latvian MFA, <http://www.mfa.gov.lv/en/news/press-releases/2013/december/13-2/>

⁸⁶ Foreign Ministers of Latvia and Azerbaijan Commend Dynamics of Political and Economic Relations, 26.04.2013, Latvian MFA, <http://www.mfa.gov.lv/en/news/press-releases/2013/april/26-1/>

⁸⁷ Latvijas ekonomiskā sadarbība ar Azerbaidžānu, Latvijas Investīciju un attīstības aģentūra, http://www.liaa.gov.lv/files/liaa/attachments/2013.08.lv_azerbaidzana_ekon.sad_.pdf

⁸⁸ Foreign Minister Rinkēvičs Welcomes Initialling of Association Agreements with Georgia and Moldova, 29.11.2013, Latvian MFA, <http://www.mfa.gov.lv/en/news/press-releases/2013/december/01-3/>

process, Foreign Minister of Latvia Edgars Rinkēvičs in October went on a working visit to Moldova. The visit was of special importance because Moldova at that time was still suffering from a Russian ban of Moldovan wines and had been warned by Deputy Prime Minister Dmitry Rogozin that Moldova's pro-Europe drive could cause it to permanently lose control over the breakaway territory of Transdnestr and lead to a more costly energy relationship with Russia, its main supplier of gas.⁸⁹ This particular step revealed that Latvia itself can take responsibility and support countries that are subjected to external pressure. This kind of diplomatic support will be an element of the utmost important for Latvia's upcoming presidency in 2015.

Starting in 2004, Latvia-Georgia relations have been close. Latvia's foreign policy makers fully understand Georgia's attempts to become a full member of the EU and NATO because just two decades ago it was on the same track. Last year was not something exceptional in Latvia-Georgia relations – relations between both actors even intensified. In 2013, several Georgian high representatives made working visits to Latvia. Last year the ministry of foreign affairs of the Republic of Latvia welcomed Foreign Minister of Georgia Maia Panjikidze, Speaker of the Parliament of Georgia David Usupashvili and First Deputy State Minister for European and Euro-Atlantic Integration of Georgia David Dondua. In all of these meetings both sides pointed out the positive dynamics in Latvia-Georgia relations. However, this did not prevent Latvian authorities from expressing their concern about particular events in Georgia. When Georgian President Mikhail Saakashvili was prevented from delivering his state-of-the-nation address, Foreign Minister of Latvia Edgars Rinkēvičs expressed alarm over the developments in Georgia, which from the perspective of the foreign ministry raised concern about the compliance with democratic values in mutual relations between Georgia's political powers. During a meeting with the speaker of the parliament of Georgia, Edgars Rinkēvičs also voiced concern over efforts to restore monuments to totalitarian dictators and mass murderers like Stalin and invited the country to get acquainted with Latvia's experience in raising awareness and building knowledge on complex historical issues.⁹⁰ In another meeting, State Secretary Pildegovičs emphasised that court proceedings should be transparent, thus precluding statements that selective justice is exercised in Georgia.⁹¹ Concerns raised by Latvian representatives indicate that both Latvia and Georgia have close relations. Either side can raise its concerns over the political developments and events taking place in each country. Latvia is interested in Georgia building closer relations with EU. Therefore, it is crucial to identify the bottlenecks for Georgia that prevent it from signing Association Agreements with EU.

Lithuania in its presidency proved that a small country can act as a strong and powerful country. Political leaders of Lithuania, especially President Dalia Grybauskaitė, were active in representing EU opinions. Even when Russia used its leverage against EaP countries, Lithuanian leaders openly criticised Russia's steps. This affected Russia-Lithuania relations at a political level as well as an economic one. Nevertheless, Lithuania continued to reach

⁸⁹ Reuters, Rogozin Warns Moldova on Relations, The Moscow Times, 05.09.2013, <http://www.themoscowtimes.com/business/article/rogozin-warns-moldova-on-relations/485526.html>

⁹⁰ Foreign Minister Rinkēvičs Supports Georgia's Aspirations to Euro-Atlantic Integration, 05.11.2013, Latvian MFA, <http://www.mfa.gov.lv/en/news/press-releases/2013/november/05-1/>

⁹¹ Foreign Ministry State Secretary Expresses Support for Georgia's Further Euro-Atlantic Integration, 20.11.2013, Latvian MFA, <http://www.mfa.gov.lv/en/news/press-releases/2013/november/20-3/>

the goals that were set before its presidency. Looking at Latvia's presidency, various challenges still remain. The most important of these is to identify the main persons who take responsibility and who are good enough to represent Latvia's position. Next year Latvia will hold parliamentary elections. The new parliament will be established only a few months before Latvia's presidency will start. And it is still uncertain what role will be played by the Latvian president, who has officially announced that the amount of money that is planned for Latvia's EU presidency is far too high, and what kind of position will be taken by the next foreign minister. These questions should be clarified between various stakeholders here in Latvia prior to Latvia's EU presidency in the beginning of 2015.

Representatives of the ministry of foreign affairs of the Republic of Latvia were active in supporting Ukraine's attempts to harmonise its political and economic systems in a way that has been implemented in the EU for many years. In the beginning of October 2013, the Latvian foreign minister welcomed his Ukrainian counterpart Leonid Kozhara to Latvia. During the meeting, both ministers signed a joint statement. In the statement the Latvian side reiterated its continuous support for the European aspirations of Ukraine. Both sides acknowledged the crucial importance of signing the Association Agreement, which includes a deep and comprehensive free trade area, during the Eastern Partnership Summit in Vilnius on 28-29 November 2013.⁹²

Nevertheless, one of the main aims in 2013 – paying direct attention to the issue of signing the Association Agreement with Ukraine – was not accomplished. Obviously this cannot be perceived as a failure of Latvia's foreign policy. The decision of the acting political elite in Ukraine to incline themselves towards Russia's proposed economic and political models was influenced by a number of events and stakeholders. Latvia itself could not change the process. However, Latvian authorities did not bring to the discussions any aspects that could be a "game changer" in EU-Ukraine relations. Latvian policy was more reactive than proactive. Like other EU leaders, Latvia strongly condemned the actions taken by Ukrainian authorities to remove protesters from the Independence Square by forceful methods⁹³ and expressed hope that Ukrainians will continue to draw closer to the EU.⁹⁴ No additional assessment of why the EU lost Ukraine and how Latvia will act to recover its previous position has been made.

The assessment of EaP progress and its importance is crucial not only externally; it is important to explain these issues domestically as well. Taking into account that one of Latvia's main priorities during its presidency will be the EaP, it is necessary to explain to the public why we have chosen these countries as a priority, what the main gains from this policy are, how we are planning to achieve our goals, and other questions. Otherwise, the lack of information promotes incomprehension in society.

In 2013, Latvia was quite successful in supporting efforts to improve EU-Belarus relations, which in recent years have struggled. Latvia tried to convince EU policy makers that

⁹² Joint Statement of Minister of Foreign Affairs of Ukraine Mr. Leonid Kozhara and Minister of Foreign Affairs of the Republic of Latvia Mr. Edgars Rinkēvičs, 02.10.2013, Latvian MFA, http://www.mfa.gov.lv/data/joint%20statement_02102013.pdf

⁹³ Foreign Ministry Strongly Condemns Cynical Actions by Ukrainian Authorities, 12.12.2013, Latvian MFA, <http://www.mfa.gov.lv/en/news/press-releases/2013/december/11-2/>

⁹⁴ Foreign Minister Rinkēvičs: Only Ukraine Itself Can Choose Its Path of Development, 17.12.2013, <http://www.mfa.gov.lv/en/news/press-releases/2013/december/17-1/>

Belarus is an important neighbour for the EU which should not be neglected. For instance, in the meeting of the Foreign Affairs Council in Luxembourg, the Latvian foreign minister explained that it was vital for both sides to contribute in an equally responsible manner to the EU-Belarus dialogue: for Belarus by improving the situation in the field of political freedoms and values; and for the EU, in view of the progress made in this area, by resuming the EU-Belarus political dialogue and activating practical cooperation in various sectors.⁹⁵ Efforts made by Latvian representatives and their like-minded partners in other EU countries resulted in Belarus's participation in the third EaP Summit in Vilnius – which was opposed by many EU leaders. Belarus's participation in the EaP is an important element of Latvia-Belarus relations. Using the sticks and carrots of the EaP initiative, Latvia is interested in closer economic relations with Belarus and the country's democratic development.

Commitments made by the Latvian Foreign Service to support the Eastern Partnership initiative were stimulated in an additional two ways. First, in the second half of the year a new position – ambassador-at-large for the Eastern Partnership – in the ministry of foreign affairs of the Republic of Latvia was established. The post of ambassador-at-large for the Eastern Partnership is held by Juris Poikāns, a career diplomat. This decision indicates that Latvia is determined to work in a systematic manner in the direction of the EaP. Secondly, on October 17 the ministry of foreign affairs launched a grant project competition to support development projects in EaP countries. The total amount of funding allocated for development cooperation projects was 25,000 lats (~35,500 euros). Although the project does not offer a large amount of money, it is a good way to stimulate cooperation between NGOs from EaP countries and Latvia in order to promote democratic norms and values in EaP countries. Both these strategies indicated that Latvia is fully focussed on the EaP. However, the success of its policy depends on many stakeholders within both the EU and the EaP. Therefore, the next part of this chapter will focus on the overall challenges for the EaP initiative, which is important to understand in shaping Latvia's policy towards the EaP.

The Eastern Partnership: challenges remain after the Vilnius Summit

The EaP initiative has an ambitious long term goal: put three Eastern Europe countries⁹⁶ and three South Caucasus countries⁹⁷ back into the EU's spotlight and open up new mechanisms for cooperation, including a multilateral dimension. It is ambitious because on the one hand most EaP countries are closely politically and economically linked with Russia, and on the other hand not all EaP countries are ready to obey and implement reforms set by EU.

Although Association Agreements between Georgia and the EU and Moldova and the EU were initialled, as well as a visa facilitation agreement signed between Azerbaijan and the EU, Vilnius summit leaders did not achieve the main goal of the year – to sign an Association Agreement with Ukraine. The inclination of Ukraine towards deeper

⁹⁵ Foreign Minister Rinkēvičs Calls for Resuming EU-Belarus Dialogue, 23.04.2013, Latvian MFA, <http://www.mfa.gov.lv/en/news/press-releases/2013/april/23-2/>

⁹⁶ Ukraine, Moldova, Belarus.

⁹⁷ Georgia, Armenia, Azerbaijan.

integration with Russia will cause several consequences to EaP competitiveness in the “zero-sum-game” that has been played in EaP territory. The EaP’s long term viability depends mainly on two aspects: first, the competitiveness of its proposed economic model with the Russia-led Custom Union, and second, visa liberalisation, which seems the biggest carrot in the hands of EU leaders and which obviously has two sides, with positive and negative implications for both EU and EaP countries.

The EaP initiative appears to be part of a wider geopolitical rivalry. In order to win tangible results in this game, players are forced to use various sticks and carrots. However, participating in this rivalry should not undermine the values and norms that are declared in the main EU documents and promoted by its member states. Therefore, first and foremost, EU leaders in the contest over the EaP must avoid a “now-or-never” approach. The EU has to be open to further cooperation and even integration only if its counterparts fully understand and apply the norms and values of the EU. Instead of rushing towards an agreement, the EU should allow Ukrainians, Moldovans, Georgians and others to define their own pace of moving forward, which may well be after the Riga summit. That will relieve some of the pressure on the EU, and will also avoid sidestepping its own values and losing credibility. Once the EaP countries meet all the conditions, then the responsibility of the EU is to ensure that the agreement is signed quickly and that the document is ratified by the European Parliament and national legislatures.

There is no consensus among the public spheres of EaP countries as to which of the proposed economic models – the EU (DCFTA) model or the Russian (Customs Union) model – would be more appropriate for their country. According to Eurasian Development Bank data, 50% of Ukrainians, 54% of Moldovans, 67% of Armenians, 65% of Belarusians, 37% of Azerbaijanis and 59% of Georgians support their respective country’s participation in the Customs Union.⁹⁸ With the exception of Azerbaijan, other EaP societies tend to support the Customs Union rather than the EU’s proposed economic model. At the same time, the societies of Georgia, Moldova and Ukraine in answer to the question of political integration are inclined towards the EU. In other words, ideologically the EU’s proposed political model seems more attractive, while economically in the short term perspective the Russia-led Customs Union can provide greater benefits to most EaP countries.

Historically, Russia’s political leaders have perceived Eastern Europe and the Caucasus as within their sphere of influence. Activities by Western organisations like the EU and NATO in the region have been considered a threat to the country. Therefore, in order to maintain influence over its neighbours, Russia has tried to use various kinds of sticks and carrots. Not all of Russia’s activities have been successful. One might even argue that, for instance, sanctions and rhetoric in the relationship with EaP countries even helps EaP entrepreneurs make the decision to move closer to the EU. However, the case of Ukraine revealed that pressure from Russia still works.

Signing the agreement – if the Eastern Partnership countries meet all the necessary requirements – will be a legally binding instrument between the EU and its eastern partners. But the signing itself won’t make those countries more European. Therefore, the

⁹⁸ Potential Member States Demonstrate High Level of Public Support for Joining the Customs Union, 24.09.2013, Eurasian Development Bank, http://eabr.org/e/press_center/press-releases/index.php?id_4=32383#.UkJsdz9AxmU.twitter

only way to counter Moscow's offer is to change the mind-set of the people through open borders and formal and informal education. From this perspective, cooperation with the non-governmental sector matters. In all six countries there are a lot of pro-European organisations that stimulate deeper integration with the EU. Cooperation with these organisations is vitally necessary.

The EU and Russia are not the only important actors in the neighbourhood, and the clever use of other external resources might be instrumental in changing the situation one way or another. For the EU, which is rather reluctant to commit its own resources, it is vitally important to cooperate and coordinate with the other stakeholders, such as NATO (admittedly, issues in EU-NATO relations may make such cooperation difficult), the United States (whose positive cooperation with Belarus on transit through the Northern Distribution Network is an example of how one ally's policy can set back efforts of the other), the United Nations, the Council of Europe, International Financial Institutions and other, less well known, mechanisms.

Peace and security, along with tackling poverty, are perceived by the populations of the EaP countries as the most important areas of cooperation between the EU and their countries. It is widely believed that the EU brings peace and stability to the surrounding regions. For instance, Armenia's abandonment of the EU integration path to secure its military and political alliance with Russia is a clear signal for the EU that greater involvement of EU institutions in resolving protracted conflicts is needed. National security concerns trumped lucrative EU trade offers, and that should be taken into account in designing future policies towards the Eastern Neighbourhood.

The Eastern Partnership beyond 2013: opportunities and tasks for the EU and Latvia

Lithuania's presidency of the EU highlighted the challenges that Latvia could face during its presidency in 2015. Lithuania during its presidency supported any EaP country's ambitions and steps towards deeper integration with the EU. This active policy and attitude raised economic and political "pressure" on the countries from Russia. There is a high possibility that Latvia during its presidency in 2015 will experience similar "pressure" from Russia. In order to be able to face the challenges raised by Russian authorities, Latvia first of all can develop a preventive communication strategy for its position in the context of the EaP. Second, in collaboration with the ministry of economics, it would be necessary to organise workshops in order to inform Latvian exporters about Russia's potential bans on Latvian goods, taking into account the Lithuanian experience. Work in these directions should already start in the beginning of the next year.

It must be noted that the overall approach of EU institutions and European leaders to promote the "attractiveness" of the EaP initiative has not been sufficiently systematic and effective. At the Vilnius Summit, for instance, President of European Commission José Manuel Barroso publicly announced that by signing an Association Agreement with the EU Ukraine will annually save 500 million euros on reduced import duties and its economy will

experience a 6% growth of its GDP.⁹⁹ Compared to Russia, the EU's public campaign before the Vilnius Summit in all EaP countries has been insufficient. There still exists a lack of understanding of the potential gains and challenges of signing Association Agreements and DCFTA among the societies of EaP countries. Therefore, Latvia as the EU president in 2015 should be able to offer (or at least initiate) a comprehensive and targeted public relations campaign in EaP partner countries.

Although Armenia has officially declared its willingness to step into the Customs Union, its participation in the EaP initiative will continue. However, together with representatives of Armenia, EU leaders have to find a new ways to cooperate with Armenia. The EU has to maintain the *more for more* principle with regards Armenia and continue to support Armenia's participation in various EU projects (LIFE, HORIZON 2020, ERASMUS +).

One of the main interest of Latvia is to keep Belarus at the negotiating table of the EaP, not excluding it from EaP group. Although Belarus is not Latvia's main trading partner, it is Latvian neighbour, with whom several economic projects have been established. The presence of Belarus at the negotiating table of the EaP should not be perceived as an end in itself. Cooperation must be based on safeguarding democratic values and norms.

Throughout 2013 it became increasingly clear that there is the need for a new "a-la carte" approach with EaP countries. In May 2012, the European Council on Foreign Relations came out with a publication titled "The EU and Azerbaijan: beyond oil". The authors proposed a "hug and hold" strategy – support Azerbaijan's economic modernisation on the condition that Azerbaijan will fulfil its commitments to reform its political and economic systems. This approach should be implemented in all EaP countries. It is obvious that financial support from the EU is of minor importance compared to the EU's "know how". The EU should support the transfer of knowledge, the exchange of programmes and capacity building in the public sector, while giving more funding to civil society initiatives and the independent media.

Next year will be crucial for Moldova's development and cooperation with the EU. In the autumn of 2014, parliamentary elections will be held in Moldova. According to the current ratings the Communist Party could gain a victory. Moldova's Communist Party has officially announced that they would prefer Moldova's development turn to the east rather than the west. Therefore, it is in the interests of the EU to sign an Association Agreement and DCFTA with Moldova as soon as possible. It is also difficult to predict how the events taking place in Ukraine will affect its development. However, the EU and Latvia itself must be ready to provide political and financial support for any kind of Ukrainian effort to come closer to the EU. Taking into account that Latvia's presidency is approaching, every action of the Latvian authorities to support the EaP countries' efforts to integrate into EU is a positive dynamic.

⁹⁹ Ian Bond, The Eastern Partnership: The Road from Vilnius Leads to ...?, 09.12.2013, <http://www.cer.org.uk/insights/eastern-partnership-road-vilnius-leads?utm>

LATVIAN-BELARUSIAN RELATIONS IN 2013: MULTIPLE REALITIES

Diāna Potjomkina

Latvian-Belarusian relations are complex, involving many players with sometimes contradictory interests. Over the years, the mood has been shifting from pragmatic friendliness to freezing and back to *détente*, sometimes taking into account external factors (such as the situation in Belarus itself and the Western position), but sometimes based on purely domestic factors. In 2013, tensions at the EU-Belarus level still played a role in Latvian-Belarusian relations. However, this year was marked by a *creeping détente* at the bilateral level – somewhat surprising if we take into account that neither the situation in Belarus nor EU policy had undergone any significant changes.

This chapter is structured as follows. Firstly, the Latvian policy planning documents relevant to Latvian-Belarusian relations are discussed, focussing on the foreign minister's 2013 foreign policy report. Secondly, the main developments in 2013 are reviewed, distinguishing between Latvia's policies bilaterally and within the broader EU/international framework, as well as among different players. Finally, some recommendations are offered for the year 2014 and beyond.

The context and official guidelines

Belarus could well be the Latvia's least discussed neighbour. In recent years it attracted somewhat greater attention in the media, but still receives but a brief mention in most policy planning documents and political debates. A country file on the Ministry of Foreign Affairs webpage appeared only recently, later than for the Bahamas and Belize.¹⁰⁰ This does not mean there is a lack of interest, though. Rather, Belarus “has been deliberately kept in the shadows by some players”¹⁰¹ in order to avoid controversies. The main source of contention here is the EU's restrictive policy towards Lukashenka's regime, which limits multilateral and bilateral business and political contacts and is perceived by many players as harmful to their interests. Since the Latvian government put forward economic growth and export promotion as the No. 1 foreign policy priority, the role of economic groups in

¹⁰⁰ Divpusējās attiecības, Latvijas Republikas Ārlietu ministrija, <http://www.mfa.gov.lv/lv/Arpolitika/divpusejas-attiecibas/>

¹⁰¹ Gatis Pelnēns, Diāna Potjomkina, “The Political Implications of Latvia's Economic Relations with Russia and Belarus” in *The Economic Presence of Russia and Belarus in the Baltic States: Risks and Opportunities*, ed. Andris Sprūds (Riga: Latvian Institute of International Affairs, Centre for East European Policy Studies, Soros Foundation-Latvia, 2012), 189.

external relations has increased further – and up to now, Latvian foreign policy has been vacillating between the long-term “European” view and short-term economic interests.

As has been discussed elsewhere,¹⁰² in Latvia’s policy towards Belarus, two major strands have co-existed since the 1990s – the “normative” (a cliché denoting a typical pro-Western, pro-democratic policy, sometimes with elements of securitising relations with Russia) and the “pragmatic” (short-term policy mainly guided by the motives of economic cooperation and profits, with some elements of ideational support for Lukashenko’s “strong hand” regime). The former has been represented by certain political forces, although some of these changed their position during the last economic crisis, and by some civil society representatives. The latter counts upon the support of some politicians and, importantly, a few big entrepreneurs, mainly from the transportation and transit sector. Taking into account the strict norms existing at the EU level, Latvian “pragmatists” have normally been more careful, if not less active. High-level political contact between Riga and Minsk did not occur until 2008, when EU-Belarusian relations improved; in line with the EU’s policy, after the non-democratic 2010 presidential elections in Belarus and ensuing violent suppression of protests, bilateral links were frozen again in 2011. However, not all Latvian players feel obliged to abide by EU standards. Latvia’s foreign policy, at least in this regard, remains insufficiently coordinated. While the Foreign Ministry tends to support joint EU policies, or at least pays lip service to them, the parliament, the president and other ministries (not speaking about municipalities) seem to enjoy comparative freedom in their actions. Also, the previous report by the foreign minister, in 2012,¹⁰³ did not give a clear indication of the principles of Latvia’s foreign policy towards Belarus (it was somewhat more pro-European in 2011¹⁰⁴).

The 2013 foreign minister’s report to the parliament showed controversies once again. There is no clear-cut vision of a Latvian-Belarusian relationship but rather a few scattered mentions, which ascribe to Belarus three distinct roles: firstly, a country whose non-democratic regime does not fully correspond to Latvia’s and the EU’s interests; secondly, a neighbour and an important trade and transit partner; thirdly, we may also mention here Latvia’s general policy towards the six Eastern Partnership (EaP) countries, which are supported in their efforts to become closer to the EU – with a strong underlying economic rationale. As a result, a careful attempt to find balance was made:

“The progress in dialogue of these [EaP] countries with the European Union remains diverse. In Belarus, in September 2012, parliamentary elections took place, and these did not comply with the OSCE standards; as a result, relations between Belarus and the European Union at the political level still remain frozen. Latvia is interested in maintaining dialogue with Belarus, because it is an important trade and transit partner. At the same time, Latvia is convinced that strengthening democracy and the market economy in

¹⁰² E.g. Gatis Pelnēns, Diāna Potjomkina, *The Political Implications of Latvia’s Economic Relations with Russia and Belarus*.

¹⁰³ [Edgars Rinkēvičs], *Ārlietu ministra ikgadējais ziņojums par paveikto un iecerēto darbību valsts ārpolitikā un par paveikto un iecerēto turpmāko darbību Eiropas Savienības jautājumos* (Rīga: LR Ārlietu ministrija, 2012), <http://www.mfa.gov.lv/lv/Arpolitika/>

¹⁰⁴ [Ģirts Valdis Kristovskis], *Ziņojums par valsts ārpolitiku un Eiropas Savienības jautājumiem* (Rīga: LR Ārlietu ministrija, 2011), <http://www.mfa.gov.lv/lv/Arpolitika/>

Belarus would provide broader opportunities for promoting cooperation in different spheres”.¹⁰⁵

One must also note that in the parliamentary debate itself Belarus played almost no role, but the speakers who touched on the topic of the Eastern Partnership had the same broad understanding of its goals.¹⁰⁶ And what do other policy planning documents say about the issue? The long-term vision of the 11th Saeima’s mandate (until the end of 2014), which was defined in 2012, supported democratisation and a European orientation of the Eastern Partnership countries, while at the same time not forgetting about trade.¹⁰⁷ The government’s Action Plan (which, some argue, hierarchically takes precedence over the foreign minister’s report) explicitly mentions Belarus only with regard to the work of the intergovernmental commission charged with economic cooperation and the border regime. The Eastern Partnership in this case is, again, seen from both a democratisation/reform and a trade perspective.¹⁰⁸ Thus, the balance is precarious. This allows for greater flexibility, but no strong guidelines exist for situations where conflicting interests are at stake. Logically, it also makes the assessment of results more difficult.

Bilateral relations in 2013

Judging against these official guidelines, how can we evaluate Latvia’s bilateral policy towards Belarus in 2013? On the one hand, as shown by Riga’s official reaction to the Russian-Belarusian “Zapad 2013” military exercises and to Belarussian criticism of “human rights violations” in Latvia, Belarus was treated rather carefully. Still, other cases show that Latvia slowly but surely tilted towards “pragmatism”, although neither the situation in Belarus nor the EU’s policies towards it changed. This is what I call *creeping détente* – an improvement in relations which mostly shows on the daily level, in small steps, without explicitly declaring a new foreign policy strategy. Short-term economic interests clearly influenced Latvia’s policy in 2013.

At the end of 2012 and the beginning of 2013 both Belarusian and Latvian officials had come forward with very explicit requests for political rapprochement, as a precondition for good economic relations. Belarusian Deputy Foreign Minister Alexander Guryanov stressed that “political guarantees” are necessary for Belarusian investment into Latvian seaport infrastructure, and pointed to, “with regret”, Latvia joining the EU’s sanctions

¹⁰⁵ [Edgars Rinkēvičs], Ārlietu ministra ikgadējais ziņojums par paveikto un iecerēto darbību valsts ārpolitikā un Eiropas Savienības jautājumos (Rīga: LR Ārlietu ministrija, 2013), <http://www.mfa.gov.lv/lv/Arpolitika/> [author’s translation]. It must be noted that this part is taken from the section of the report which deals with the year 2012, but it evidently refers to 2013 as well. Belarus was not directly mentioned among Latvia’s plans for 2013, while relations with the EaP states were planned in line with the above.

¹⁰⁶ Latvijas Republikas 11. Saeimas ziemas sesijas trešā sēde 2013. gada 24. janvārī, Latvijas Republikas Saeima, <http://www.saeima.lv/lv/transcripts/view/153>

¹⁰⁷ [Edgars Rinkēvičs], Ārlietu ministra ikgadējais ziņojums par paveikto un iecerēto darbību valsts ārpolitikā ... (2012).

¹⁰⁸ Valdības rīcības plāns Deklarācijas par Valda Dombrovskā vadītā Ministru kabineta iecerēto darbību īstenošanai (apstiprināts ar Ministru kabineta 2012. gada 16. februāra rīkojumu Nr. 84) [as of 17.12.2013], Latvijas Republikas Ministru kabinets, <http://www.mk.gov.lv/lv/mk/darbibu-reglamentejosie-dokumenti/ricibas-plans-dv/>

against Belarus.¹⁰⁹ (As one can remember, Latvia in fact vocally, and successfully, opposed/watered down EU economic sanctions in 2012 and took pride in the issue). In turn, Minister of Transport Aivis Ronis (who, for unrelated reasons, resigned in January 2013) made a sort of pledge in an interview:

“We look at Belarusians as at our neighbours, regardless of who is in the Latvian government and who holds the power in Minsk. [...] The Latvian government will *never* agree to such economic sanctions against Belarus which have repercussions for our own people, our jobs in Latvia. [...] I hope that the president of Belarus, Alexander Lukashenko, appreciates Latvia’s position towards Belarus up to now and the fact that, predictably, it will remain the same in the future”.¹¹⁰

This sort of political pressure evidently was related to the subsequent improvement of relations. According to the Belarussian ambassador, indeed relations started to improve at the end of 2012. Belarus continued to demand better political relations during 2013 and warned of possible economic consequences in a “stick and carrot” tone.¹¹¹ Once again, this proved that Latvian politics is prone to the direct influence of politico-economic interests, especially due to the prolonged economic crisis.

Overall, in 2013 economics was the main topic of bilateral talks, and sometimes the only one. For instance, it could be expected that official press releases would refer to all aspects of Latvian-Belarussian relations, including the problematic ones. However, this was not exactly the case, and some announcements left the impression that Belarus is a completely “normal” neighbour with no fundamental differences from Estonia or Lithuania. Admittedly, the MFA was more moderate, but the Ministries of Economics and Transportation, and less predictably the Saeima (parliament), were remarkably “pragmatic” in their rhetoric and policies.

On 10 April 2013, Minister of Foreign Affairs Edgars Rinkēvičs paid a working visit to the Belarussian city of Vitebsk, which was the first visit at such a level since 2010, and met with his Belarussian counterpart, Vladimir Makei. (From 2008-2010, both prime ministers and foreign ministers exchanged visits, but this happened during the aforementioned thaw in EU-Belarussian relations; in 2011 and 2012, high-level diplomatic contact virtually came to a halt). The main focus in the talks, according to official announcements, was markedly “pragmatic” – the development of economic contacts, especially trade, transport and transit; cooperation among municipalities; cross-border cooperation; bilateral legal agreements; and cultural exchange. The ministers also discussed possibilities to further improve the already very beneficial agreement on simplified travel for border area residents.¹¹² In a nutshell, these are the current Latvian priorities in relations with Belarus. They are rather unproblematic, and indeed also beneficial for the Belarussian population

¹⁰⁹ Ольга Львовская, Белорусско-латвийские отношения становятся все крепче, Бизнес & Балтия, December 6, 2012, <http://www.news.lv>

¹¹⁰ Anita Daukste, Aivis Ronis: jaunā politiskā sezona vieš satraukumu, Neatkarīgā Rīta Avīze Latvijai, December 19, 2012, <http://www.news.lv> [author’s italics].

¹¹¹ Juris Paiders, Gerasimenko: Mēs esam ieinteresēti attīstīt sadarbību tranzīta jomā, Neatkarīgā Rīta Avīze Latvijai, April 9, 2013, <http://www.news.lv>; see also Александр Федотов, Александр Герасименко: Белорусский экспорт работает на экономику Латвии, Бизнес & Балтия, 1st July, 2013, <http://www.news.lv>

¹¹² Edgars Rinkēvičs: Latvija ir gatava sekmēt dialogu starp ES un Baltkrieviju, 10.04.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/Jaunumi/zinas/2013/aprilis/10-04-02/>

(especially regarding people-to-people contacts), as long as they do not overshadow other concerns. To the credit of the MFA, in this case the issue of transparency in Russian-Belarusian military exercises was raised as well as EU-Belarus dialogue. Still, the mere occurrence of a meeting at such a level is remarkable. (An additional bilateral meeting between E. Rinkēvičs and V. Makei took place on the margins of the EU Foreign Affairs Council in July, but no information on its content is available).¹¹³

A string of contacts just below the ministerial level continued throughout the year. In February, the Latvian Ambassador met V. Makei; in the press release, only “pragmatic” issues are mentioned.¹¹⁴ In March, the State Secretary of the Latvian MFA, Andrejs Pildegovičs, visited Minsk, meeting with both V. Makei and Deputy Foreign Minister Alena Kupchyna (as well as with EU ambassadors and independent Belarusian experts). In this case, not only the practical issues but also the problems for EU-Belarus dialogue were addressed.¹¹⁵ A. Pildegovičs and A. Kupchyna met again during the Riga Conference in September, but in this case no disagreements or moot points were recorded.¹¹⁶ Finally, in November, a new Belarusian ambassador was accredited; on the occasion of her meeting with the foreign minister, both sides again focussed just on improving economic, and now also political, cooperation.¹¹⁷ (Almost the same was said during the farewell visit of the previous ambassador, with the difference that democracy and human rights were mentioned as a prerequisite for EU-Belarusian dialogue).¹¹⁸ One must also note that business contacts proliferated, often with support of the MFA or the Latvian Embassy. For instance, the Embassy advertised the Business Club of Latvian Entrepreneurs, which works in Latvia (established in 2009);¹¹⁹ numerous seminars, forums and informative events were organised and/or attended (e.g. in the fields of business, tourism and science).¹²⁰ The MFA thus evidently supported, or even overtook, the functions of other branch ministries and state agencies, with economics as the first priority.

The MFA is of course the leading institution in Latvia’s foreign policy, but the decisions of other players also contribute to bilateral relations and the overall image of the country. In

¹¹³ Latvia: Eastern Partnership should focus more on democracy and visa liberalization issues, 23.07.2013, The Baltic Course, http://www.baltic-course.com/eng/baltic_states_cis/?doc=78138

¹¹⁴ Vēstnieks M. Popkovs ar Baltkrievijas ārlietu ministru pārrunā divpusējo attiecību aktualitātes, 07.02.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/belarus/jaunumi/zinas/2013/02-07/>

¹¹⁵ Ārlietu ministrijas politiskais direktors tiekas ar Baltkrievijas ārlietu ministru, 14.03.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/jaunumi/zinas/2013/marts/14-5/>

¹¹⁶ Valsts sekretārs A. Pildegovičs tiekas ar Ukrainas, Moldovas un Baltkrievijas ārlietu ministru vietniekiem, 06.09.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/jaunumi/zinas/2013/septembris/06-6/>

¹¹⁷ Ārlietu ministrs E. Rinkēvičs tiekas ar jauno Baltkrievijas vēstnieci Latvijā M. Dolgopolovu, 22.11.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/jaunumi/zinas/2013/novembris/22-3/>

¹¹⁸ Ārlietu ministrs Edgars Rinkēvičs tiekas ar Baltkrievijas vēstnieku Aleksandru Gerasimenko atvadu vizītē, 14.10.2013, <http://www.mfa.gov.lv/lv/jaunumi/zinas/2013/oktobris/14-7/>

¹¹⁹ Vēstniecībā Minskā tiekas Baltkrievijā strādājošie Latvijas uzņēmēji, 24.05.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/belarus/jaunumi/zinas/2013/05-24/>

¹²⁰ E.g. Aļona Zandere, Izlauzties cauri protekcioņismam, Diena, September 5, 2013, <http://www.news.lv>; Minskā prezentē Latvijas tūrisma produktus, 25.09.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/belarus/jaunumi/zinas/2013/09-25-2/>; Vēstnieks M. Popkovs informē Latvijas uzņēmējus par iespējām Baltkrievijā, 04.09.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/belarus/jaunumi/zinas/2013/09-04/>; Vēstnieks M. Popkovs Latvijas-Baltkrievijas Zinātniskā Forumā uzsver veiksmīgo ekonomisko sadarbību, 26.09.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/belarus/jaunumi/zinas/2013/09-26/>

2013, the Saeima was quite active in the Belarusian direction, and unlike the MFA it focussed almost only on practical issues. Firstly, the parliamentary cooperation group did not show any restraint in cooperating with the Belarusian regime and their undemocratically elected counterparts in Minsk. This can be primarily explained by the heavy predominance of *Harmony Centre* MPs, but, notably, members of traditionally more sceptical factions such as VL-TB/LNNK, *Reform Party* and *Unity* (and ZZS) also participated in bilateral visits. At least four meetings took place during the year: a trilateral meeting with the participation of Estonia in Tallinn in February;¹²¹ an official visit of the parliamentary cooperation group's delegation to Minsk in September, in which all five factions currently working in the parliament were represented – the MPs met not only their colleagues but also the Belarusian Deputy Minister of Economy;¹²² a “non-political” visit of the Saeima's ice hockey team to Minsk in October – the Belarusian team in the “friendship game” was led by A. Lukashenko; and an informal meeting of the chairs of the Belarusian and Latvian parliamentary cooperation groups, also in October.¹²³ And secondly, the Saeima speaker, Solvita Āboltiņa, maintained very positive and pragmatic rhetoric with no reservations.¹²⁴ All of these created the impression that Belarus is an absolutely natural cooperation partner, but such rhetoric did not fit the overall position of the EU. Brussels does not, in principle, recognise the Belarusian parliament (and the European Parliament even called for a boycott of the 2014 Ice Hockey World Championship in Minsk). Here, one can also remember an interview with the president of Latvia, Andris Bērziņš, in which he openly noted that democracy in Belarus will not be coming anytime soon, but this in no way should preclude economic cooperation.¹²⁵ Thus, non-MFA officials created a somewhat different face of Latvian policy towards Belarus.

This was the political side of the story, but we must also remember the major events dedicated to trade, logistics and cooperation among municipalities. In May, the second bilateral forum of sister cities took place in the Latvian border city of Daugavpils – with almost 300 representatives from more than 50 Latvian and Belarusian municipalities taking part. Interestingly, in the press it also appeared as the “entrepreneurship forum”.¹²⁶ In July, the topic was taken further at a meeting between the state secretary of the Latvian Ministry of Environmental Protection and Regional Development and the Belarusian deputy minister of economics.¹²⁷ And in October, the 9th meeting of the Intergovernmental Commission (IGC) was held, where both ministers of economics acted as co-chairs. The IGC

¹²¹ Елена Лазарева, Десять лет как один день, Вести Сегодня, 8th July, 2013, <http://www.news.lv>

¹²² Latvijas parlamentārieši viesojas Baltkrievijā, 10.09.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/belarus/jaunumi/zinas/2013/09-10/>

¹²³ Валерий Зайцев, С Белоруссией можно и нужно работать!, Вести Сегодня, 18th October, 2013, <http://www.news.lv>

¹²⁴ E.g. Āboltiņa Baltkrievijas vēstniekam: abas valstis vieno cieša sadarbība ekonomikā, 04.06.2013, LR Saeima, <http://www.saeima.lv/lv/aktualitates/tiksanas-un-vizites/21050-aboltina-baltkrievijas-vestniekam-abas-valstis-vieno-ciesa-sadarbiba-ekonomika>

¹²⁵ Aigars Freimanis, Andrejs Panteļejevs, Nav tik daudz jāsapņo, bet vienkārši ir jārēķina, Diena, March 4, 2013, <http://www.news.lv>

¹²⁶ Latvijas un Baltkrievijas sadraudzības pilsētu pārstāvji tiksies forumā Daugavpilī, 16.05.2013, <http://www.mfa.gov.lv/lv/belarus/jaunumi/zinas/2013/05-16/>; Ilze Upīte, Pilsētas svētkus veltīs uzņēmējiem, Neatkarīgā Rīta Avīze Latvijai, 17th April, 2013, <http://www.news.lv>

¹²⁷ Minskā pārrunā Latvijas un Baltkrievijas reģionu attīstības perspektīvas, 16.07.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/belarus/jaunumi/zinas/2013/07-16/>

reviewed the whole spectrum of bilateral economic relations, including transportation, transit, communications, various manufacturing sectors, research, investments, joint enterprises, tourism, cross-border cooperation projects and the like. Announcements to the press, again, left an overwhelmingly positive impression – even on those issues where in reality Latvian-Belarusian cooperation does not develop actively or easily (like investment or the use of Latvian seaports).¹²⁸ All of these were showcased, by the officials and the press, as major steps forward in bilateral cooperation. It is also interesting that, apart from economics and related fields, another big topic in the MFA's communication about bilateral relations was cultural exchange,¹²⁹ which helped to provide a certain balance between economic and “high politics” issues. It also shows a certain tendency towards depoliticising relations with Belarus.

What were the cases in which the Latvian side maintained a critical position towards its neighbour? First and foremost, criticism was expressed concerning the Belarusian-Russian Zapad 2013 military exercises, which were held from September 20-26, with the participation of approximately 13,000 troops from both countries.¹³⁰ The Latvian MFA started voicing concern about the exercises already in February. The scenario was unknown for a long time, and it was suspected that, like in the previous exercises of this kind, Russia and Belarus might practice an attack on the Baltic States and Poland. The MFA, in this context, called for greater transparency – which in the end was provided, so that observers from Latvia and other states could monitor the exercises.¹³¹ Latvia itself set an example by inviting Belarus to observe the NATO *Steadfast Jazz* exercises held on its territory. However, the MFA also remained careful when it became known that the topic of exercises would be countering an attack of hostile external forces in order “to overthrow the Belarusian socio-political system”,¹³² and criticised the negative impact of the exercises on regional security.¹³³ Latvian Minister of Defence Artis Pabriks even went so far as to declare that the exercises did not have defence as the main objective.¹³⁴ One can discuss the wording of particular announcements, but in general this caution was well-advised. Latvia has to take into account the ever closer cooperation between Russian and Belarussian armies (including a plan to develop a joint missile defence system) and Russia's generally uncooperative stance on international security issues. And it is clear that the current Belarusian regime is not an outpost against Russia – on the contrary, A. Lukashenko has

¹²⁸ Par Latvijas – Baltkrievijas Starpvaldību komisijas sēdē panāktajām vienošanām, 23.10.2013, LR Ekonomikas ministrija, <http://em.gov.lv/em/2nd/?cat=621&id=33577>

¹²⁹ The Belarusian minister of culture visited Riga in March. See Latvijas un Baltkrievijas attiecības, 31.10.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/Arpolitika/divpusejas-attiecibas/Baltkrievija/>

¹³⁰ Uldis Ķezberis, Militārie manevri Zapad biedē kaimiņus, Diena, September 19, 2013, <http://www.news.lv>

¹³¹ Ārlietu ministrijas komentārs par šogad gaidāmajām stratēģiskajām Baltkrievijas un Krievijas militārajām mācībām “Zapad-2013”, [27.02.2013.], LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/jaunumi/komentari-presei/27-02-2013/>

¹³² Anna Maria Dyer, “The Russian-Belarusian “West 2013” Military Exercise: An Alliance against External Enemies?”, PISM Bulletin No. 102 (555), 27th September 2013, www.pism.pl/files/?id_plik=14832

¹³³ E.Rinkēvičs vērs uzmanību uz militāro mācību „Zapad 2013” negatīvo ietekmi Baltijas un Ziemeļu reģionā, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/jaunumi/zinas/2013/septembris/26-1/>

¹³⁴ BNS, Krievijas vērienīgajām mācībām ‘Zapad 2013’ nav aizsardzības mērķi, norāda Pabriks, 20.09.2013, Delfi, <http://www.delfi.lv/news/national/politics/krievijas-verienigajam-macibam-zapad-2013-nav-aizsardzibas-merki-norada-pabriks.d?id=43670945>

been bringing his country closer and closer to it. Riga also issued a harsh statement on the Belarusian report of alleged human rights in Latvia¹³⁵ – which, again, resembled Russian tactics.

As has been mentioned before, Latvian-Belarusian economic relations actually are not as rosy as many public statements show. Transit, in particular, is heavily politicised and seems to be marred not only by international disagreements but also by internal ones. Belarus, and Latvian players that have a stake in it, have successfully used transit as an instrument of political pressure, sometimes quoting exorbitantly high figures. For several years Belarus has been indicating that it is interested in renting or acquiring seaport infrastructure in Latvia (the “carrot”) or, on the contrary, reorienting its cargo towards Russian or other ports (the “stick”) – of course, this depends not only on purely economic factors but also on political relations. The fact that in April 2013 Belarus acquired 30% of a Klaipeda terminal was quoted as a positive example of Belarus’s commitment.¹³⁶ Latvian players such as the Latvian Railways,¹³⁷ the Employers’ Confederation and harbours have been historically supportive of tight cooperation with Belarus, at least in words. And, among others, in 2013 Latvia put its hopes into the ZUBR project – a container train going through Belarus and now, as planned, to Turkey and Ukraine (this project was also endorsed by the IGC).¹³⁸ However, these seemingly positive aspects are underlaid by numerous problems.

Some of the reasons that the benefits of economic cooperation with Belarus are often overestimated are related to the different ways of calculating statistics. Proponents of “good relations” tend to quote data in their favour, e.g. that cargo between Belarus and Latvia provides 56% of all traffic on Latvian Railways, that trade volume in 2012 reached 764.7 million euros or even \$3.4 billion,¹³⁹ or that in Latvia, more than 1,500 joint ventures with Belarusian capital operate.¹⁴⁰ (And one may remember that in 2012 the potential impact of EU economic sanctions against Belarus was, at first, grossly exaggerated). Without doubting the importance of Latvian-Belarusian economic cooperation, these figures still have to be put in context. And it shows that many cargoes actually do not originate in Belarus but are in transit from Russia and other CIS countries (meaning that Belarus has “no merit” in this case) – overall, the Belarusian share in Latvian transit is

¹³⁵ Baltkrievijas Ārlietu ministrija ziņojumā par cilvēktiesību pārkāpumiem pasaules valstīs apgalvo, ka Latvija ir starp tām valstīm, kurās ar varasiestāžu palīdzību tiek izdarīts spiediens uz žurnālistiem. Vai Ārlietu ministrijai nav par šo kas sakāms, proti, vai tiešām Latvijā ar varasiestāžu palīdzību tiek izdarīts spiediens uz žurnālistiem?, [02.06.2013.], <http://www.mfa.gov.lv/lv/jaunumi/komentari-presei/02-06-2013/>

¹³⁶ Juris Paiders, Gerasimenko: Mēs esam ieinteresēti attīstīt sadarbību tranzīta jomā, Neatkarīgā Rīta Avīze Latvijai, 9th April, 2013, <http://www.news.lv>

¹³⁷ See e.g. Juris Paiders, Latvijas dzelzceļam rekordgads, Neatkarīgā Rīta Avīze Latvijai, 22nd January, 2013, <http://www.news.lv>

¹³⁸ Par Latvijas-Baltkrievijas Starpvaldību komisijas sēdē panāktajām vienošanām, 23.10.2013, LR Ekonomikas ministrija, <http://em.gov.lv/em/2nd/?cat=621&id=33577>; Andris Bērziņš: „Latvijai un Turcijai ir visas iespējas paplašināt veiksmīgo sadarbību un kopīgi meklēt jaunus virzienus ekonomikas attīstībai un valstu labklājībai”, 02.04.2013, http://president.lv/pk/content/?cat_id=603&art_id=20587

¹³⁹ Александр Федотов, Александр Герасименко: “Белорусский экспорт работает на экономику Латвии”.

¹⁴⁰ Egons Mudulis, Baltkrievi grib piedalīties tranzīta procesā, Dienas Bizness, 28th October, 2013, <http://www.news.lv>

about 24%.¹⁴¹ Belarus, in 2012, was only eighth in Latvia's overall trade turnover, being responsible for 1.99% of Latvian exports and 4.05% of Latvian imports. The amount of bilateral trade has changed, and indeed slightly increased, over the years, but without any profound differences between the "thaw" and the "freeze" periods in political relations.¹⁴² The figure of \$3.4 billion was calculated by taking into account goods not originating in Belarus but coming into Latvia through its territory – the Belarusian Ambassador himself admitted this fact.¹⁴³ Moreover, taking into account both trade in services and in goods, it can be seen that Latvia indeed has a positive balance in services (+59.6 million euros), but this is more than outweighed by the negative balance when trading in goods (–266.52 million euros in 2012).¹⁴⁴ This imbalance is most likely explained by the relatively closed nature of the Belarusian market to Latvian businesses. And when we look at the actual amount of bilateral investment, it can be seen that indeed these have increased steadily since 2004, but in 2012 Belarus still accounted only for 0.2% of all FDI into the Latvian economy (29th place).¹⁴⁵ While the absolute numbers may, at first, sound impressive, the percentages show that Belarus, by most accounts, will not play a role in the Latvian economy similar to that of Lithuania or Estonia anytime soon.

Other problems concern the style of doing business that is characteristic of Belarus. Latvian official representatives have actually warned entrepreneurs of certain negative aspects of the neighbouring country, such as heavy interference of the state in the economy, protectionism and red tape.¹⁴⁶ Entrepreneurs themselves sometimes acknowledge the possibilities Belarus provides but also voice concern over the politico-economic situation, the impact of the Customs Union, administrative difficulties and the lack of adequate protection, etc.¹⁴⁷ The fact that Belarus, after several years of discussion, still has not acquired Latvian seaport infrastructure is sometimes explained by problems on the Latvian side, but the alternative explanation is the extremely low prices offered by the Belarusians. (It has also been noted that Belarusian investments into Klaipeda, which were mentioned above, came in the form of promises of future supplies, not hard currency).¹⁴⁸ The same has been said about the railway – that is, transit prices desired by Belarusians would be below the actual production value for the Latvian side.¹⁴⁹ Belarus also has an interest in creating joint ventures with Latvian companies – which might sound

¹⁴¹ Андрей Каратаев, От перевозок к сборке, Бизнес & Балтия, 6th December, 2012, <http://www.news.lv>; Александр Федотов, Александр Герасименко: "Белорусский экспорт работает на экономику Латвии".

¹⁴² Latvijas un Baltkrievijas attiecības, 31.10.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/Arpolitika/divpusejas-attiecibas/Baltkrievija/>

¹⁴³ Александр Федотов, Александр Герасименко: "Белорусский экспорт работает на экономику Латвии".

¹⁴⁴ Latvijas un Baltkrievijas attiecības, <http://www.mfa.gov.lv/>. Over the first three quarters of 2013, Latvian exports of goods to Belarus rose by approximately 3.5%, but imports fell by approximately 23% – author's calculations from AT05. Eksports un imports pa harmonizētās sistēmas sadaļām un valstīm latos – Sadaļas, Valsts, Gads, Periods un Preču plūsma, LR Centrālā statistikas pārvalde, <http://ej.uz/44hj>

¹⁴⁵ Informācija par Latvijas ārējo tirdzniecību: Baltkrievija, LR Ekonomikas ministrija, <http://em.gov.lv/em/2nd/?cat=30288&id=23461>

¹⁴⁶ Aļona Zandere, Izlaupties cauri protekcionismam, Diena, 5th September, 2013, <http://www.news.lv>

¹⁴⁷ Uldis Andersons, Mazliet biedējošā iespēju zeme, Dienas Bizness, 22nd May, 2013, <http://www.news.lv>; Uldis Andersons, Nekā pārdabiska, ja kārtīgi iepazīst, Dienas Bizness, 22nd May, 2013, <http://www.news.lv>

¹⁴⁸ Egons Mudulis, Alkst pēc sadarbības, Dienas Bizness, 28th October, 2013, <http://www.news.lv>

¹⁴⁹ Egons Mudulis, Kaimiņattiecības sarežģītas, Dienas Bizness, 28th August, 2013, <http://www.news.lv>

beneficial, but this is also how Belarus aims to reduce its own costs and avoid paying foreign (that is, Latvian) businesses.¹⁵⁰ Another example of what business with Belarus can be like was offered by the notorious tender for the acquisition of trams in the city of Daugavpils. The city, after some setbacks, decided to sign a contract with a Belarusian factory, which could not honour its commitments on time. The issue became highly politicised, including speculation that if the Latvian side decided to break the contract, it would leave a negative impact on Belarusian transit through Latvia.¹⁵¹ In general, it seems that Belarus uses all possible leverages for manipulating Latvian political and public opinion in its own interests, without any significant or reliable offers on its own side. These tactics are typical of the Lukashenko regime and have been employed elsewhere.

Latvian-Belarusian relations in the EU context

The previous section on Latvian-Belarusian relations may seem more surprising when put into a European Union context. Admittedly, Latvia is not the only member state sceptical of the EU's stance, and the EU's policies are not as strong and coherent as they could have been. Still, over the years the EU has amassed a sufficiently detailed basis of norms regarding this neighbouring country. The Belarusian issue may have been relegated to the background since the 2010 events, but still, throughout 2013 the EU's restrictions on contact with Belarus remained virtually intact.

The mainstream approach in the EU is “more for more, less for less” – meaning that authoritarian countries like Belarus, which do not respect basic human rights, fundamental freedoms or free market rules, should receive only limited assistance and political attention. After the 2010 events, the EU stepped up its (still severely insufficient) funds for Belarusian civil society and froze contact with government representatives. By the beginning of 2013, a visa ban and asset freeze was imposed on 243 individuals. In addition, the EU introduced an arms embargo and froze the assets of 32 Belarusian companies (some more were taken off the list by interested EU members).¹⁵² Throughout 2013, it continued to criticise Belarus on issues such as the death penalty and other violations, and in October 2013 the sanctions were rolled over for the next year with only minor changes – the list now includes 232 persons and 25 entities.¹⁵³ In June, evidently in view of the November Eastern Partnership Vilnius summit, the EU suspended (but not lifted indefinitely) the travel ban on V. Makei, one of the key personalities in the 2010 repressions, but expressly stated that this “does not reflect any change in the EU's policy towards Belarus”.¹⁵⁴ Makei actually visited Brussels in July, but maintained demands for the EU's assistance without any commitments on the Belarusian side.¹⁵⁵ Understandably, this was not the ideal strategy to achieve changes in EU-Belarusian relations. And at the Vilnius

¹⁵⁰ Egons Mudulis, Baltkrievi grib piedalīties tranzīta procesā, Dienas Bizness, October 28, 2013, <http://www.news.lv>

¹⁵¹ Egons Mudulis, Alkst pēc sadarbības, Dienas Bizness, 28th October, 2013, <http://www.news.lv>

¹⁵² European Commission, ENP Package – Belarus, MEMO/13/244, 20.03.2013, http://europa.eu/rapid/press-release_MEMO-13-244_en.htm

¹⁵³ EU extends restrictive measures against Belarus, 31.10.2013, http://eeas.europa.eu/delegations/belarus/press_corner/all_news/news/2013/20131031_en.htm

¹⁵⁴ Council of the European Union, Luxembourg, 24 June 2013, 11371/13, PRESSE 279, <http://ej.uz/j58f>

¹⁵⁵ Uladzimir Dzenisevich, Breaking the Ice with Belarus: Mission Impossible?, 29.07.2013, <http://beyondthe.eu/?p=1581>

summit, the unresolved Belarusian problem was generally overshadowed by Ukraine. V. Makei appeared at the summit, but again, with no significant results. In the final declaration, Belarus appeared only in the context of visa liberalisation (it had, finally, declared a willingness to enter into dialogue with the EU on this issue¹⁵⁶); energy dialogue and nuclear safety; sectoral dialogue in the fields of economics, finance, the environment and education (these were endorsed); as well as the European Dialogue on Modernisation with Belarusian Society (“exchanges are ongoing between the EU and the Belarusian government with a view to determining the best future form of cooperation on modernisation issues”).¹⁵⁷ The results were meagre despite the evident willingness of the Lithuanian EU presidency to develop relations with the existing Belarusian regime.

Latvia, for its part, remained an active advocate of “engagement” with Belarus at the EU level – as the foreign minister was quoted saying, “We need to look for points of cooperation in the fields of economics, education and culture. More productive work, less conflict”.¹⁵⁸ Sometimes the conditions which Belarus has to meet were mentioned, sometimes not. Latvia also focussed on the steps Belarus had (allegedly) taken in order to restore dialogue with Brussels, or its readiness to do it, rather than on the shortcomings. It seems that Riga competed with Vilnius for the role of Belarus’s greatest ally. Latvian-Lithuanian competition for Belarusian cargoes and other economic opportunities has been going on for years, and in 2013 Lithuania evidently tried to use its EU presidency to change the balance in its own favour. Latvia, for its part, acknowledged the common EU position on numerous occasions,¹⁵⁹ but also actively tried to shape it according to own preferences – the pragmatic vision described above. This is not a new strategy, since Latvia’s approach to the Eastern Partnership initiative, and EU foreign policy as such, has always been rather instrumental.

One example here is Latvia’s position with regard to the European Dialogue on Modernisation with Belarusian Society (DoM). Originally launched in 2012, this initiative now excludes the Belarusian government. Officially Belarus is of course interested in EU financial aid, but in order to take part in the DoM, it has to fulfil the European political preconditions, namely the release and rehabilitation of political prisoners. The Belarusian government also demanded the “exclusion of civil society and political opposition from the Dialogue”,¹⁶⁰ which is not acceptable to the EU. Thus, although the possibility of the Belarusian government’s membership in the DoM was discussed, no real progress took

¹⁵⁶ Adrienne Warren, After Vilnius: Andrei Sannikov on Belarus’ “Awkward Attempt” at the Eastern Partnership, 30.11.2013, <http://eastbook.eu/en/2013/11/material-en/news-en/after-vilnius-andrei-sannikov-on-belarus-awkward-attempt-at-the-eastern-partnership/>

¹⁵⁷ Joint Declaration of the Eastern Partnership Summit Eastern Partnership: The Way Ahead, http://president.lt/en/press_center/press_releases/joint_declaration_of_the_eastern_partnership_summit.html

¹⁵⁸ Quoted in: Ivars Bušmanis, Grib labākus kaimiņus, Latvijas Avīze, December 2, 2013, <http://www.news.lv> [author’s translation]. See also e.g. E.Rinkēvičs aicina atjaunot ES-Baltkrievijas dialogu, 23.04.2013, <http://www.mfa.gov.lv/lv/jaunumi/zinas/2013/aprilis/23-1/>

¹⁵⁹ See also Latvijas un Baltkrievijas attiecības, 17.09.2013, <http://www.mfa.gov.lv/lv/Arpolitika/divpusejas-attiecibas/Baltkrievija/>

¹⁶⁰ Andrei Yahorau, Yury Chavusau, The Eastern Partnership Roadmap to the Vilnius Summit. Belarus: Assessment May 2012 – October 2013, [http://www.eap-csf.eu/assets/files/Articles/Web/Roadmapreports/Belarus%20roadmap%20monitoring%20csf%20nov%202013%20\(3\).pdf](http://www.eap-csf.eu/assets/files/Articles/Web/Roadmapreports/Belarus%20roadmap%20monitoring%20csf%20nov%202013%20(3).pdf)

place.¹⁶¹ Latvia's position in this regard has been, in general, supportive of Belarus. On numerous occasions, Latvia voiced support for Belarus's official participation in the DoM, without publicly mentioning any preconditions.¹⁶² Another example would be Latvia's support for bringing the EU-Belarus dialogue to a higher level. Latvia supported the temporary lifting of sanctions on V. Makei, and the Latvian Foreign Minister suggested inviting his counterpart to the meeting of EaP foreign ministers in July,¹⁶³ where V. Makei actually took part. Riga was also supportive of broadening relations with Belarus as an external partner of the Baltic Sea Region Strategy framework, which is yet another example of pro-dialogue orientation.¹⁶⁴ The parliament (at the level of the speaker) voiced a similar position to the MFA – generally very supportive of the EU-Belarus dialogue but with some reservations.¹⁶⁵ The president, meanwhile, seemed to consider the EU an obstacle which must be overcome, so that no restrictions are imposed on relations with Belarus.¹⁶⁶ For the sake of balance, one can remember the fact that Latvia voiced concern about the new Belarusian nuclear power plant in Ostrovets,¹⁶⁷ where it was indeed important to show solidarity with Lithuania. As shown above, Latvia also raised the issue of the Zapad 2013 exercises at the international level, so it did not look like an unprincipled supporter of dialogue with the Lukashenka regime. The previous negative experience, in which Latvia became notorious for opposing economic sanctions against influential Belarusian players, also must have contributed to more careful rhetoric if not policy. Still, it can be seen that for Latvian policy-makers, pressure from the various sides was not easy to reconcile.

Conclusions and recommendations

In 2013, Latvia, like some other EU countries, continued to muddle through its relations with Belarus, not being able to take any decisive steps. Belarus is a difficult case. Many players in Latvia seem to understand both the international context and the perils that cooperation with Lukashenko's regime can bring to Latvia. At the same time, certain groups with a particular interest in Belarus – above all, business interests, but also the diaspora and some loyalists – continued to exercise strong pressure on Latvian policy-

¹⁶¹ See e.g. Gunnar Wiegand: Rehabilitation of political prisoners remains necessary condition, 25.09.2013, <http://www.charter97.org/en/news/2013/9/25/76298/>

¹⁶² E.g. Valsts sekretārs A.Pildegovičs tiekas ar Ukrainas, Moldovas un Baltkrievijas ārlietu ministru vietniekiem, 06.09.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/Jaunumi/zinas/2013/septembris/06-6/>; Latvijai prioritārie jautājumi Īrijas prezidentūras laikā. 2013.gada pirmā puse, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/Arpolitika/eu/Prioritates/irijas-prezidentura/>

¹⁶³ E.Rinkēvičs aicina atjaunot ES-Baltkrievijas dialogu, 23.04.2013, <http://www.mfa.gov.lv/lv/Jaunumi/zinas/2013/aprilis/23-1/>

¹⁶⁴ Ārlietu ministrs E. Rinkēvičs: Baltijas jūras reģiona stratēģija ir paraugs citiem Eiropas reģioniem, 22.10.2013, <http://www.mfa.gov.lv/lv/Jaunumi/zinas/2013/oktobris/22-1/>

¹⁶⁵ E.g. Āboltiņa: Latvijai un Baltkrievijai kā kaimiņiem ir daudz kopīgu jautājumu, 07.12.2011., <http://www.saeima.lv/lv/par-saeimu/saeimas-darbs/saeimas-priekssedetaja-solvita-aboltina/saeimas-priekssedetajas-aktualitates-2/19120-aboltina-latvijai-un-baltkrievijai-ka-kaiminiem-ir-daudz-kopigu-jautajumu>

¹⁶⁶ Valsts prezidents akreditē jaunus vēstniekus, 03.12.2013, LR Valsts prezidents, http://president.lv/pk/content/?cat_id=605&art_id=21536

¹⁶⁷ Vēstnieks Bahtijors Hasans akreditējas Starptautiskajā Atomenerģijas aģentūrā Vīnē, 23.10.2013, LR Ārlietu ministrija, <http://www.mfa.gov.lv/lv/Jaunumi/zinas/2013/oktobris/23-2/>

makers. As the state continues to tackle the consequences of the financial crisis, simplified arguments used by “pragmatic” players (“Latvian jobs” vs. seemingly abstract or false “human rights concerns”) still find resonance. Admittedly, more difficult problems, such as the Zapad 2013 exercises, were raised by Latvia at an international level, but generally the EU was perceived as a hindrance/obstacle to “neighbourly” Latvian-Belarusian relations. As a result, in Latvia’s foreign policy Belarus took on multiple identities – an EaP state (positive/neutral), a potentially aggressive Russian ally (negative) and a neighbour and trade/transit partner (positive). The overall approach was rather ambiguous, at times criticising Belarus and at times granting virtually unconditional cooperation. But the development of bilateral relations in practice is more telling than rhetoric, and intensive contact at both the highest and administrative levels show that Latvia has developed relations with Belarus without much restraint.

This author’s argument is that Latvia’s position towards Belarus should, in the future, be more principled and oriented towards the long term. Economic relations, of course, are important, and cooperation between neighbours is, to a great extent, natural. At the same time, Belarus is a problematic partner. It is unreliable and can be easily used for achieving Russian goals; the main goal of the government in Minsk is to find political and financial resources for preserving and legitimising its rule, without much regard for its partners’ needs. Belarus is heavily protectionist, and its economic problems could cause problems for Latvian businesses at any time. To a great extent, the Belarusian regime has been able to survive for so long thanks to its ability to manoeuvre between Russia, the EU and other players on the international arena, trying to extract assistance in return for promises which later are not kept. Russia is the main sponsor of the current regime, so in no case should A. Lukashenko be considered a bulwark against Russian influence. At the same time, the previous détente in relations with the EU brought no positive changes in Belarus and only limited, if any, benefits for Latvia.

In this context, the interests of Latvia and the EU as a whole should be to promote liberalisation and a truly European orientation in Belarus, so that it moves towards a more sustainable economic and socio-political model. One should not be afraid of negative consequences either now or in the future. Belarus is in fact heavily dependent on the EU, and in particular, cooperation with Latvia is possibly more important for the Belarusian than for the Latvian side. Belarus can reorient its economic activities away from EU partners, but only at its own peril. Moreover, the longer the current situation persists, the more painful will be the transition, both for Belarusians and for Europeans. The current regime in Minsk, by now, is sure that limitations imposed by the EU can be easily overcome, and it is not interested in real reforms. The EU should be demonstrating a strong and coherent stance towards Belarus, and should work more on overcoming its own collective action problems (which admittedly is a challenging task not only for external relations).

Right now, the most important task for Latvia is preparing for the EU Council Presidency in the first half of 2015 and the Riga Eastern Partnership summit in particular. In the EU, a certain “Eastern partnership fatigue” has taken place, and this tendency could strengthen after the Vilnius summit. In this context, Latvia has the chance to gain a reputation as an honest broker in relations with partner countries, including Belarus, and to offer new guidelines and principles. Working at the international level not only is a necessity for

Latvia as the holder of the future EU presidency, it is also best suited to Latvia's needs. In order to make its policies more efficient and attractive for all its member states, the EU itself will have to make changes. This means, inter alia, developing better expertise on Belarus, committing more resources, refocussing and controlling the existing aid flows, and adapting internal decision-making procedures. But this means serious work at analysing the situation on the ground. For instance, taking into account the Belarusian tradition of the "social contract", a good strategy would be "non-political" visibility projects in the Belarusian regions, providing training in foreign languages, other sorts of education, realising small infrastructure investments and the like. This would help to promote a European orientation in the Belarusian society, without creating unneeded political controversies. In the economic field, possibilities for enhanced cooperation and experience exchange between small and medium sized enterprises should be explored, while links with large state-controlled Belarusian businesses must be avoided due to potential political and economic consequences. Visa liberalisation is a must and should not be subject to the wishes of the partner government, especially when the partner is a closed autocratic regime. And while developing its presidency priorities, Latvia should be prepared for the pressure which was directed against Lithuania to be repeated. Greater openness and better communication with all stakeholders and society at large is a must – it is necessary for implementing high-quality policies and for preventing corrupt deals.

At the same time, Latvia should focus on niches where it can cooperate with Belarus and at the same time build its reputation at the international level. Lithuania has already been specialising on issues such as scholarships for Belarusian students, Poland on the mass media. For Latvia, education, science, languages and translation, and analysis (including the analysis of legal norms in the context of Eurasian integration) could all be prospective fields. The analysis of EU assistance instruments is yet another field where Latvia could contribute its expertise. Riga also has to review its internal and external communication, focussing not so much on the abstract "human rights vs. economics" debate but on the possible consequences of different policies towards Belarus (which is also relevant for the EU at large). It is also important for Latvia to continue to work at strengthening grassroots contacts. Just as Lithuania and Poland attract large numbers of Belarusians, and their money, with shopping opportunities, Latvia could think of possibilities for people-to-people relations. And yet another issue would be to identify all existing possibilities and formats for attracting and coordinating donors' help. In particular, when preparing for the presidency in 2014, it may be beneficial to develop a coalition of likeminded states, joining efforts with Sweden, Poland and Germany in particular. In general, the coordination of policies is important at both the domestic and the international level. Again, taking into account the limited resources available to Latvia, it is important to think beyond purely bilateral relations.

LATVIA'S PARTNERSHIP WITH COUNTRIES IN CENTRAL ASIA: RISKS AND OPPORTUNITIES

Anna Beitāne

Central Asia is considered one of the most promising directions for Latvia's foreign policy agenda during its EU rotating presidency in 2015.¹⁶⁸ There are several principal reasons for this: firstly, the geopolitical importance of Central Asia, which is strategically located at the crossroads of two continents (i.e., Asia and Europe) and surrounded by some of the world's fastest-growing economies such as India and China; secondly, the EU's growing vulnerability and dependency on Russian energy sources¹⁶⁹ as well as the need for a diversified energy supply policy in order to increase energy security;¹⁷⁰ thirdly, the need to prevent instability and drug trafficking that could lead to far-reaching consequences for the region, including the EU;¹⁷¹ and finally, the slow progress on human rights, good governance, the rule of law and democratisation in Central Asia.

Taking into account these considerations, this essay will seek to examine Latvia's current economic and political partnership with Central Asia (particularly focussing on Kazakhstan¹⁷² and Uzbekistan¹⁷³ due to their growing importance in Latvia's economic and

¹⁶⁸ Foreign policy priorities for 2013 – preparation for EU Presidency and support to euro adoption, 24.01.2013, Latvian Ministry of Foreign Affairs, <http://www.mfa.gov.lv/en/news/press-releases/2013/january/24-2/>

¹⁶⁹ This is particularly relevant to the Baltic States, where Russia is the sole gas supplier.

¹⁷⁰ Central Asia is often seen as an alternative energy supplier due to its significant hydrocarbon resources and favourable geopolitical location for transport routes to European markets. Together with Russia, Kazakhstan, Turkmenistan and Uzbekistan possess the world's second largest reserves of oil and gas. Moreover, both Kazakhstan and Uzbekistan have significant quantities of uranium, with the former constituting the world's third largest producer of uranium and a major supplier to the EU. Central Asia: What Role for the European Union, International Crisis Group, Asia Report No. 113, 10.04.2006, 3.

¹⁷¹ Events in Afghanistan, Iraq, and elsewhere proved that chronically unstable regions serve as ideal havens for terrorist and criminal groups. For the most part, borders in Central Asia are poorly demarcated, and there is little to prevent people or groups from crossing illegally. Moreover, the region suffers from its strategic location at the centre of global narcotics flows. Traffickers have reopened old silk trade routes to transport opiates from Afghanistan into the Central Asian republics, which are then sent on by air, rail or car to Russia and the EU. Central Asia: What Role for the European Union, 8-9.

¹⁷² Trade data shows that Latvia is Kazakhstan's leading trade partner in the Baltic States, while Kazakhstan is Latvia's leading trade partner in Central Asia. Kulpash Konyrova, Central Asian States Eye Latvian Ports, NewEurope, 13.04.2013, <http://www.neweurope.eu/article/central-asian-states-eye-latvian-ports>

¹⁷³ Uzbekistan sees Latvia as one of its chief trade partners in the European Union: mutual trade turnover between the countries grew by almost 20% in 2012. Anete Jēkabsons, The Baltic States and Central Asia, EUCAM, European National Policies Series, Iss. 11, March 2013, 1-4.

trade relations) and its efforts to resolve the abovementioned issues. The main method used in this essay is data analysis. The data sources include the EU's policy documents, normative and legal acts; publications by individual researchers; current news from international organisations and think tanks; and interviews and speeches by relevant European and Central Asian political and public figures.

The essay will be structured in the following way. The first part will provide a brief synopsis of the EU's and Latvia's overall strategy towards Central Asia, highlighting the progress that has been made since the 2007 Strategy for a New Partnership with Central Asia. The second part will turn to a case study analysis and look at Latvia's current partnership with Kazakhstan, whereas the third part will examine Latvia's relations with Uzbekistan. The final part will evaluate the costs and benefits of Latvia's relations with the Central Asian republics and outline potential scenarios for Latvian-Central Asian relations in the medium-term on the basis of the analyses discussed in the previous parts.

At the outset some limitations should be set. The essay does not claim to contain an exhaustive list of the risks and opportunities of Latvia's partnership with Kazakhstan and Uzbekistan, or the only possible scenarios of future interaction between Latvia and the Central Asian republics. Instead, it aims to leave the debate open, and welcomes further discussion and contributions. Furthermore, in addressing these themes and drawing them together, the analysis does not engage in a detailed manner with several related issues that are important in their own right, such as a detailed examination of the benefits of the Northern Distribution Network (NDN). Finally, there is a lack of prior detailed (secondary) research on Latvia's partnership with Central Asia; as a result, this study has relied largely on primary sources such as interviews, the EU's policy documents, normative and legal acts, and current news from international organisations and think tanks.

The EU's (and Latvia's) strategy towards Central Asia

From 1991 to 2001, there was hardly a country which paid any attention to the activities of the five newly emerged governments in Central Asia: Russia was fully preoccupied with its domestic political and economic turbulence, the US with the redefinition of its *grand strategy* towards the new world order, and Europe with its sudden undivided status.

The 9/11 attacks and the invasion of Afghanistan, as well as the 'global war on terror', played a decisive role in reshaping the strategy towards Central Asia by global powers, including the EU. Elements such as the strategic location of Central Asia to host military bases and the links between some Islamic activists and the Afghan conflict, which could help to avoid a spread of the conflict, made Central Asia the new 'heartland'.¹⁷⁴ The 2006 and 2009 gas crises between Ukraine and Russia also made the EU revitalise its energy security policy and brought its attention to the 'possible' alternative energy supplier – Central Asia – with its significant hydrocarbon resources.¹⁷⁵ As a result, this led to the European Council's decision to elaborate an EU (Political) Strategy for Central Asia, which would be adopted under the German EU Presidency.

¹⁷⁴ Laurène Aubert, *The European Union's Policy towards Central Asia and South Caucasus: A Coherent Strategy?* Bruges Regional Integration and Global Governance Papers, 2012, 8.

¹⁷⁵ *Ibid.*

“The EU and Central Asia: Strategy for a New Partnership”, adopted in June 2007, marked a real breakthrough in relations between European and Central Asian countries both at a bilateral and multilateral level.¹⁷⁶ The document made an attempt to focus more on defining European interests in the region, finding prospective areas for cooperation, and improving the approach to the region by making it more effective instead of drawing up another assistance programme with generic developmental goals based on the perceived needs of the region.¹⁷⁷

In this respect, the Strategy has reinforced EU cooperation with the five states on major issues facing the region, such as poverty reduction, sustainable development and stability, which formed the core of the programme for 2007-2013. Moreover, the document helped to fully involve Central Asia in the EC regional and inter-state programmes as equal partners with the other CIS countries, candidate countries and new EU Member States in strategic areas such as energy, transport, the environment and education.¹⁷⁸ Central Asian countries have subscribed to the TRACECA multilateral agreement on transit and transport, the INOGATE Umbrella Agreement, the EC-supported Environment for Europe Process and the EU Water Initiative for Eastern Europe and Central Asia.¹⁷⁹ They have been keen to adapt their higher education systems to the principles of the Bologna Process and bring them in line with the Lisbon Agenda, in particular through the TEMPUS and the ERASMUS Mundus programmes and participation in the 7th Framework Programmes for research and technological development.¹⁸⁰ All these EU programmes gave a new impetus through support for political dialogue mechanisms and new initiatives set up under the ENP, the Eastern Partnership and the EU Central Asia Strategy.¹⁸¹

In the forthcoming years, the Strategy envisages an intensification of political ties (regular dialogue on a variety of topics with top officials), more assistance (double the amount/budget for the period of 2007-2013), and a strong emphasis on bilateral relations.¹⁸²

When speaking about Latvia’s partnership with Central Asia, it could be argued that Latvia and the five Central Asian states have managed to establish positive and stable political relations. In past decades, economic and trade relations between the Central Asian republics and Latvia relied heavily on logistics and transit services due to their common transportation infrastructure inherited from the Soviet era – most importantly, the rail network.¹⁸³ However, the far-reaching effects of the 2008/9 economic recession on the global economy combined with the contrasting rise of the economic credibility of developing global powers (such as China, India, Brazil and Kazakhstan) made Latvia search for new business partners beyond the EU and develop alternative investment projects in

¹⁷⁶ Nargis A. Kassenova, “View from the Region” in Neil J. Melvin, *Engaging Central Asia: The European Union’s New Strategy in the Heart of Eurasia* (Centre for European Policy Studies: Brussels, 2008), 122-3.

¹⁷⁷ *Ibid.*

¹⁷⁸ V. A. Maldonado, *Central Asia DCI Indicative Programme (2011 – 2013)*, European Commission External Relations Directorate General, Directorate Eastern Europe, Southern Caucasus, Central Asia Republics (Brussels, 2013), 18.

¹⁷⁹ *Ibid.*

¹⁸⁰ *Ibid.*

¹⁸¹ *Ibid.*

¹⁸² Nargis A. Kassenova, “View from the Region”, 122-3.

¹⁸³ Anete Jēkabsonsone, *The Baltic States and Central Asia*, 1.

the areas of trade, energy security, science and education. In this respect, the post-recession period has brought a new phase in Latvia's partnership with Central Asia. In general, most major and promising bilateral projects are still linked to transit, but opportunities in technology transfer, agriculture, tourism and education are also being discussed and explored. The Baltic States are all interested in developing alternative energy supply routes via the Caspian Sea, but they are not directly involved with Central Asia's energy market.¹⁸⁴

Another layer that ties together Latvia and Central Asia is security, mostly because of the Northern Distribution Network (NDN), which is used to transfer supplies from Baltic ports through Central Asia and the Caucasus to Afghanistan. The supply route has strategic importance for the Baltic countries due to its economic and security aspects as well as through international credibility, especially in light of the NATO withdrawal from Afghanistan in 2014. In the future it could serve as a focal point for creating new trade and transit opportunities. However, this possibility does not feature highly on the current agenda and will depend on the future security and stability of Afghanistan. Thus, Central Asia is perceived by Latvia as a challenging yet promising region.¹⁸⁵

Political and intergovernmental relations have also been developed and strengthened: all three Baltic countries have embassies in Central Asia. Latvia was the first country to open an embassy in Uzbekistan in 1992, which also covers Tajikistan, Turkmenistan, Kyrgyzstan and Afghanistan.¹⁸⁶ In 2004, Latvia opened an embassy in Kazakhstan with the goal of increasing bilateral trade and investment capabilities in the country. All these efforts resulted in high-level visits at the parliamentary and presidential level, which included the sharing of the experience and mechanisms of the Baltic countries' parliamentary and democratic processes with the Central Asian countries.¹⁸⁷

Latvia fully supports the efforts of the European Union and the Organisation for Security and Cooperation in Europe (OSCE) in promoting common liberal values such as democracy, human rights and the rule of law in Central Asia. At the same time, however, Latvia's primary bilateral interests are emphasised as increasing trade and improving economic ties. In this respect, Latvia is not particularly vocal on promoting democracy, human rights or rule of law issues during bilateral, intergovernmental visits, for fear of endangering their trade partnerships. Moreover, Latvia does not have enough financial or human resources to engage in bilateral development assistance or human rights programmes in Central Asia. Instead, Latvia makes an indirect contribution through bringing national experts in to work and engage in the OSCE or EU frameworks, or through increasing development cooperation in specific areas such as justice reform.¹⁸⁸

Latvia also has engaged with Central Asia on 'soft' security issues such as border management, training and the rule of law, mostly within the framework of the OSCE, the UN or the EU Border management programme in Central Asia (BOMCA).¹⁸⁹ So, in general, it

¹⁸⁴ Anete Jēkabsons, *The Baltic States and Central Asia*, 1.

¹⁸⁵ *Ibid.*

¹⁸⁶ *Ibid.*, 1-2.

¹⁸⁷ *Ibid.*

¹⁸⁸ *Ibid.*

¹⁸⁹ *Ibid.*, 3.

could be argued that a large progress has been achieved in cooperation with Central Asia at a European and regional level.

Latvia's partnership with Kazakhstan

A top-ten oil producer, and rich in other natural resources, Kazakhstan has attracted billions in foreign investment and advanced a foreign policy that makes it a vital bridge between Europe and Asia.¹⁹⁰ Hence, it is not surprising that Kazakhstan is often seen by European policymakers and international experts as the most promising partner for cooperation in Central Asia. Kazakhstan owes this favourable status not simply to its rapid level of economic development and certain political freedoms 'permitted' by the relatively authoritarian regime, but also to its commitment to promote an active engagement in international affairs and build a multi-ethnic and multi-confessional secular state in which Kazakh would be the national language, but in which Russian would remain a language of international communication.¹⁹¹

This willingness to participate in international relations and promote global cooperation could be explained by the fact that Kazakhstan was initially disadvantaged by being landlocked. To compensate, it has taken advantage of all the bilateral and multilateral funding available for infrastructure improvements. These improved Kazakhstan's logistics capabilities and made the country an important transportation corridor in NATO's Northern Distribution Network, supporting military operations in Afghanistan.¹⁹² Moreover, Kazakhstan inherited the world's fourth largest nuclear arsenal. President Nursultan Nazarbayev's decision to give up these weapons brought him international stature. Now Kazakhstan makes all possible efforts to strengthen and maintain its international presence: the first success was when the country became Chairman-in-Office of the Organisation for Security and Cooperation in Europe (OSCE) in 2010, hosted the OSCE Summit in December of that year and was the founder of the CICA (Conference on Interaction and Confidence Building Measures in Asia). The next accomplishment was hosting the 7th Asian Winter Games in January-February 2011. Astana also successfully outbid Liege (Belgium) to become the venue of Expo 2017. Moreover, in 2013 President Nazarbayev and Kazakhstan's leadership laid out an ambitious agenda to make Kazakhstan one of the 30 top economies in the world by 2050.¹⁹³

All these factors make Kazakhstan an important partner for Latvia (due to our shared Soviet legacy and economic potential) and this is why cooperation between the EU and the Central Asian countries is seen as one of the top priorities during Latvia's EU rotating presidency in the first half of 2015. In this respect, it could be argued that 2013 was an especially fruitful year in terms of strengthening economic relations and maintaining an active political dialogue between the two countries at all levels: the highlight of this cooperation was the president's visit to Kazakhstan in June 2013 along with five government ministers and more than 60 business people.

¹⁹⁰ Martha Brill Olcott, Kazakhstan at 20, Diplomatic Courier, Carnegie Endowment For International Peace, 12.12.2011, <http://carnegieendowment.org/2011/12/20/kazakhstan-at-20/8kfl?reloadFlag=1>

¹⁹¹ Ibid.

¹⁹² Ibid.

¹⁹³ N.Khamitova, President Outlines Domestic, Foreign Policy Priorities in Meeting with Ambassadors to Kazakhstan, The Astana Times, No.1 (22), 23 January 2013, 1, 3.

The most promising sector of cooperation is trade relations: trade data shows that relations between Latvia and Kazakhstan are developing steadily. Currently, the total volume of trade between the two countries is €112 million. The main areas of cooperation are transit, education and tourism. Communication technologies, agriculture and environment protection, science, pharmacy and healthcare are also considered as important areas of cooperation.¹⁹⁴

However, at the core of Kazakhstan's partnership with Latvia lies geopolitical and strategic importance: geographically, Latvia is a country with access to the sea, with the major sea ports of Riga, Ventspils, and Liepaja that can handle different cargoes. Kazakhstan needs access to European markets and the open seas for its main export goods – crude oil, gas, and grain.¹⁹⁵ That is why President Nazarbayev pointed out that “access to the Baltic Sea through the ports of Latvia is of special importance to Kazakhstan”.¹⁹⁶ Indeed, Kazakhstan has already been actively present in the Baltic ports of Latvia since the middle of the past decade. It ships its grain to world markets through the port of Ventspils and its ferroalloys transit runs through the free port of Riga. Nevertheless, only recently (thanks to Latvia's membership in the EU and Kazakhstan's booming economy) did both countries see the opportunity to expand their cooperation in this area even further by creating new and, to some extent, innovative projects that could increase the mutual goods turnover to half a billion US dollars. This could be done by utilising the transit capabilities of Kazakhstan and Latvia to transport goods between China and Europe, and this ambitious project seems possible as the joint stock company National Company Kazakhstan Temir Zholy (KTZ) is considering establishing a land bridge between the ports of Riga and Lianyungang.¹⁹⁷

Kazakhstan and Latvia have maintained the successful cooperation of their countries within various international organisations, including the UN, as well in the dialogue which is progressing between the EU and Kazakhstan as Kazakhstan tries to join the World Trade Organisation. Progress has also been made in the area of peacekeeping and conflict management between the two parties: recently Adilbek Dzhaksybekov, the minister of defence of the Republic of Kazakhstan, met with Juris Maklakovs, the extraordinary and plenipotentiary ambassador of Latvia to Kazakhstan, to discuss prospects for bilateral cooperation within the framework of the “Partnership for Peace” programme, with a special emphasis on the development of Kazakhstan's peacekeeping capacity of the armed forces.¹⁹⁸ The “Steppe Eagle” peacekeeping exercise, which is conducted every year in Kazakhstan by military officers and representatives of foreign countries in the framework of NATO's Individual Partnership Action Plan for Kazakhstan, presents a good platform for interaction and cooperation between Latvia and Kazakhstan in the areas of defence, security and counterterrorism.¹⁹⁹

Latvia and Kazakhstan have also sustained a strong cultural and educational bond. Kazakhstan actively participates in the ERASMUS Mundus framework, and currently there

¹⁹⁴ Kulpash Konyrova, Central Asian States Eye Latvian Ports.

¹⁹⁵ *Ibid.*

¹⁹⁶ *Ibid.*

¹⁹⁷ *Ibid.*

¹⁹⁸ Kazakhstan Defence Minister, Latvian Ambassador Discuss Development of Kazakhstan Armed Forces' Peacekeeping Potential, BNews, 27.02.2013, <http://bnews.kz/en/news/post/126546/>

¹⁹⁹ *Ibid.*

are over 100 Kazakh students studying at Latvian higher education establishments. All in all, cooperation between the countries remains strong, but it is preoccupied with trade and transit agreements. However, there are some prospects for widening relations to other promising and innovative areas such as science, technology and environmental protection. (See the section *Risks and Opportunities*).

Latvia's partnership with Uzbekistan

Uzbekistan is the most populous country in Central Asia, with significant amounts of natural resources, including oil, gas and gold.²⁰⁰ It is an important strategic partner for Afghanistan-bound North Atlantic Treaty Organisation traffic – a partner that seeks to maintain good relations with European nations. At the same time, Uzbekistan is known for its neutrality and willingness to remain independent of the bigger nations to become a regional power in its own right.

Our shared Soviet history and later cooperation in the NDN framework helped both Latvia and Uzbekistan to establish good, working relations over the past 22 years. The past year is no exception: it was particularly productive in terms of establishing important interstate treaties and intergovernmental agreements, as well as maintaining intensive political dialogue in the sphere of transport and communications (including automobile and other international shipping), education, science, agriculture, accreditation and metrology, information technologies, tourism and other areas.²⁰¹

Particular attention has been paid to the creation of a sustainable and normative foundation for fostering economic dialogue. For instance, agreements on economic and industrial cooperation, on the protection of investments, as well as on avoiding double taxation are already in force between the two states.²⁰² Moreover, Latvia is among the three largest trading partners of Uzbekistan in the European Union. In 2012, bilateral trade between the two countries amounted to more than \$240 million.²⁰³ Mutual trade between

²⁰⁰ Uzbekistan was the third largest natural gas producer in Eurasia, behind Russia and Turkmenistan, in 2011. Moreover, Uzbekistan has 594 million barrels of proven crude oil reserves as of January 2013. Country Analysis Note, EIA, US Energy Information Administration, August 2013.

²⁰¹ During the past year several important agreements were signed, including an agreement between the government of the Republic of Latvia and the government of the Republic of Uzbekistan on co-operation in health care and medicine, a memorandum of understanding between the transportation ministry of the Republic of Latvia and the ministry of foreign economic relations, investments and trade of the Republic of Uzbekistan on co-operation in transport and the transit of goods; a memorandum of understanding between the economics ministry of the Republic of Latvia and the ministry of foreign economic relations, investments and trade of the Republic of Uzbekistan on steps to be taken to expand bilateral trade relations; an agreement between the ministry of environmental protection and regional development of the Republic of Latvia and the state committee on environmental protection of the Republic of Uzbekistan on co-operation in the area of environmental protection; and a co-operation programme for 2014-2016 between the foreign ministry of the Republic of Latvia and the foreign ministry of the Republic of Uzbekistan. On 11 October 2013, a memorandum of understanding was signed by the state agency for tourism development of the Republic of Latvia and the Uzbekturizm National Company of the Republic of Uzbekistan on co-operation in the area of tourism. The Latvian-Uzbek Partnership Has an Outstanding History, with Much Potential for New Opportunities, 17.10.2013, Latvijas Valsts Prezidents (President of Latvia), http://www.president.lv/pk/content/?art_id=21330&lng=en

²⁰² UzA, Anvar Babayev, Uzbekistan, Latvia Embark on New Phase of Cooperation, Uzbekistan National News Agency, 18.10.2013, <http://uza.uz/en/politics/3809/>

²⁰³ Uzbekistan, Latvia to Discuss Current Bilateral Relations, TREND News Agency, 17.10.2013, <http://en.trend.az/regions/casia/uzbekistan/2201736.html>

Latvia and Uzbekistan increased by 45% during the first half of 2013 in comparison to same period last year. There are now 343 joint ventures between businesspeople from the two countries.²⁰⁴ Investment cooperation has been expanding as well. To date, 22 enterprises with Latvian investment are operating in Uzbekistan, while more than 40 entities have been opened in Latvia with the involvement of Uzbek companies. They specialise in sectors such as manufacturing furniture, confectionaries, the textile industry, oil reprocessing, publishing, logistics, wholesale trade and services.²⁰⁵

In this respect, it could be argued that Uzbekistan and Latvia wield remarkable potential in the economic sphere. This argument could be backed by the results of the participation of Uzbek companies in the international exhibition Riga Food 2013, which took place last September. As part of that exposition alone, contracts and agreements worth more than 100 million dollars were inked for the supply of fruits and vegetables from Uzbekistan to Latvia and other European nations.²⁰⁶ One month later a business forum took place in Riga as part of the state visit of the president of Uzbekistan. This served as a platform for discussing opportunities for joint business and investment projects in Latvia and Uzbekistan, new areas of cooperation, the development of logistics capabilities in Latvia in the interests of Uzbekistan, and the food export industry in Uzbekistan oriented to consumers in Latvia.²⁰⁷ Finally, in November 2013, a business forum for entrepreneurs from Uzbekistan and Latvia took place in Tashkent's International Business Centre. It was organised with the purpose of further expanding Uzbek-Latvian trade and economic and investment cooperation. It was attended by the heads of ministries and other representatives and officials from government agencies, companies and corporations from the two countries responsible for foreign economic ties, trade, investment, transport and transport communications, logistics, banking and finance, education, the food industry, tourism, pharmaceuticals and the textile industry.²⁰⁸

Uzbekistan and Latvia boast immense cooperation potential in agriculture, tourism, science, education and healthcare. The Uzbek side is interested in the attraction of Latvian travel industry entrepreneurs, and in the exchange of expertise for training specialists in this sphere.²⁰⁹

Cooperation in the cultural sphere and education is also expanding steadily. Contacts have been established between the Alisher Navoi State Academic Grand Theatre of Uzbekistan and the Latvian National Opera House. Regular art and photo exhibitions, film days and concerts have been organised, while folk groups from the two countries take part in various cultural events held in Uzbekistan and Latvia. Notably, musicians from Latvia participated in the Sharq Taronalari International Music Festival in Samarkand. Especially significant has been the interaction in the education sphere. Uzbekistan comes fifth in terms of the number of international students attending Latvian higher education

²⁰⁴ Latvian, Uzbek Partnership Has Outstanding History ..., <http://www.president.lv/>

²⁰⁵ Anvar Babayev, Uzbekistan, Latvia Embark on New Phase of Cooperation.

²⁰⁶ Ibid.

²⁰⁷ Ibid.

²⁰⁸ Nodira Manzurova, The Uzbek-Latvian Business Forum, Uzbekistan National News Agency, 14.11.2013, <http://uza.uz/en/society/3841/>

²⁰⁹ Anvar Babayev, Uzbekistan, Latvia Embark on New Phase of Cooperation.

institutions. Some 200 young people from Uzbekistan currently study in Latvian universities.²¹⁰

Constructive and regular consultations are established between the foreign affairs ministries of the two countries. The two parties are interested in combating terrorism, extremism and drug trafficking in the region. Latvia and Uzbekistan work together successfully within international institutions. Latvia supports Uzbekistan's accession to the World Trade Organisation, because membership therein confirms economic maturity and helps to attract additional investments.²¹¹

In general, it could be argued that both sides made large progress in economic, political and cultural relations and there are more prospects for expanding this cooperation to other sectors and industries.

Risks and opportunities for future cooperation

Taking into account the abovementioned considerations, it could be argued that Latvia has an immense potential for developing relations and expanding its partnership with both Kazakhstan and Uzbekistan even further. In the areas of trade, transit and communications, Kazakhstan and Uzbekistan are both interested in increasing transportation volumes with Latvia. Uzbekistan and Latvia also agreed in the future to increase and diversify trade and joint investment projects, as well as to establish the creation of modern high technology companies.²¹² The two countries are interested in making more efficient use of international transport corridors and creating more favourable conditions for foreign trade shipments. Kazakhstan has also expressed interest in working with Latvia on developing technologies in the processing industries. Moreover, Prime Minister Akhmetov pointed out that Kazakhstan would like to expand cooperation in light industry, wood processing, furniture making and agricultural products, which are of particular importance to Kazakhstan at this time.²¹³ Furthermore, Latvia is planning to take part in an exhibition at the world level – Expo 2017 in Astana, which represents a good opportunity to showcase the achievements of Latvian companies by selecting and representing the most promising industries: this could serve as a great platform for increasing contacts with business partners in Kazakhstan and around the world.

Inter-parliamentary cooperation could also be expanded in the future, especially in education-sector partnerships. Latvia can offer high-quality education in music and the arts, and it also has a long-established collaboration with Kazakhstan's technical, medical and air navigation institutes, partially due to its capacity to offer a curriculum and teaching assistance in Russian.²¹⁴

At an international level, the common goal of achieving stability and prosperity by means of peaceful interaction makes Latvia and its Central Asia partners ripe for increased cooperation. The development and consolidation of stable, just and open societies that

²¹⁰ Ibid.

²¹¹ Latvian, Uzbek partnership Has Outstanding History..., <http://www.president.lv/>

²¹² Anvar Babayev, Uzbekistan, Latvia Embark on New Phase of Cooperation.

²¹³ Latvia Seen as Kazakhstan's Strategic Partner in Baltic Region, 06.06.2013, *Latvijas Valsts Prezidents (President of Latvia)*, http://www.president.lv/pk/content/?art_id=20851

²¹⁴ Anete Jēkabsons, The Baltic States and Central Asia, 3.

adhere to international norms could bring the partnership between Latvia and the Central Asian states to full fruition.²¹⁵ Good governance, the rule of law, human rights, democratisation, education and training are key areas where Latvia could share experience and expertise: Latvia's first-hand experience of transition from the Soviet political and legal system, as well as our subsequent reforms in terms of good governance and the rule of law, represent a wealth of knowledge from which the Central Asian states could benefit.²¹⁶ Latvia and the Central Asian republics also have the potential to develop cooperation in the security and regional cooperation sector, including the areas of border management, migration, the fight against organised and international crime, as well as human, drugs, and arms trafficking.

The dependency of the EU (including the Baltic States) on external energy resources and the need for a diversified energy supply policy open further possibilities for cooperation between Latvia and Central Asia. Efforts to strengthen local energy markets could help to improve investment conditions, increase energy production and efficiency in Central Asia, and diversify the energy supply and distribution in the region.²¹⁷

On the other hand, Latvia should take into account possible challenges that may arise when it deals with the Central Asian states, these being:

- transitional issues surrounding the post-Soviet states (the 'fragile' political culture, which includes weak institutions, infrastructure, problems at the socio-economic and educational level, as well as challenges for civil society and an independent media);²¹⁸
- the low level of regional cooperation and coordination between the Central Asian republics;
- extremism (the presence of terrorist organisations);
- the high level of corruption;
- the financial mismanagement of international donors;
- rigid competition;
- an unpredictable investment climate;
- complex trade policies that are badly coordinated and lack transparency (the high costs of poor transport and transit conditions, delays at border crossings, and onerous administrative and clearance requirements).

Kazakhstan appears the most stable and in fact does not exhibit many of the key dynamics summarised above. Long-term risk factors include issues of the succession of political leadership and Kazakhstan's dependency on a high oil price: if the current bubble collapses, the country would lose its major revenue source, with severe economic and social consequences.²¹⁹ Uzbekistan, on other hand, is the Central Asian state most likely to

²¹⁵ The EU and Central Asia: Strategy for a New Partnership, European Dialogue, <http://www.eurodialogue.org/eu-central-asia-strategy/10>

²¹⁶ The EU and Central Asia: Strategy for a New Partnership, <http://www.eurodialogue.org/>

²¹⁷ Ibid.

²¹⁸ Guli I.Yuldasheva, "The Northern Distribution Network and Central Asia" in Northern Distribution Network: Redefining Partnerships within NATO and Beyond, eds. Andris Sprūds and Diāna Potjomkina (Rīga: Latvian Institute of International Affairs, 2013), 93-115.

²¹⁹ A.Matveeva, Central Asia: A Strategic Framework for Peacebuilding, International Alert, Eurasia Programme (London: Nuffield Press, February 2006), 45.

experience serious political turbulence: local civil society organisations, independent media and religious groups, which have a restricted and diminishing space to operate freely in Uzbekistan, could challenge the legitimacy of Uzbekistan's current regime. Currently, the authorities seem unable to modernise economic policies and to communicate effectively with the people. Significant groups may finally lose patience, and could turn to radical action. Triggers could lie in economic issues, in disunity within the security sector, or in disaffection among the elite.²²⁰ At the same time, the abovementioned issues could be resolved peacefully through increased cooperation in strengthening intergovernmental cooperation and investment in human capital in the region, and Latvia could offer this expertise.

To conclude, Latvia has begun to take a closer look at Central Asia and at the business opportunities that are available in the region, especially in Kazakhstan. In general, bilateral relations with both Uzbekistan and Kazakhstan are strongly focussed on building and developing trade cooperation in areas such as agriculture, pharmaceuticals and shipbuilding.²²¹ In this respect, it could be stated that Latvia has immense potential to expand economic relations with the two countries, and the mutual goods turnover between the parties backs this argument. Education and tourism are also considered to be promising areas of cooperation, with good foundations due to the common *lingua franca* and inherited infrastructure networks from Soviet times. Latvia is also interested in diversifying energy supplies and improving energy security, and perceives Central Asia, with its vast energy resources, as a potential alternative energy supplier. However, it would be difficult to gain leverage in this area as it does not depend on bilateral relations with Central Asia.²²²

There are several risks and challenges that Latvia should take into account when it deals with the Central Asian states, such as weakness of the political culture, corruption and a lack of transparency. Nevertheless, the abovementioned issues could be resolved through increased intergovernmental cooperation and investment in social capital in the region, which Latvia could offer: it has valuable experience in moving from a rigid Soviet system of governance, rule of law and a state-regulated economy to democracy and open market economies. Currently, this knowledge is underestimated due to the focus on trade relations. Hence, Central Asia could be perceived by Latvia as a complex yet promising region for cooperation.

²²⁰ A. Matveeva, *Central Asia: A Strategic Framework for Peacebuilding*, 46.

²²¹ Anete Jēkabsons, *The Baltic States and Central Asia*, 3.

²²² *Ibid.*

LATVIA AND CHINA IN 2013: THE DAWN OF THE EAST AND PERCEPTIONS IN LATVIA

Mārtiņš Daugulis

If we go through the calendar of 2013 and look for real events in relations between Latvia and China, there are not so many points to outline. There is logical continuation of Latvia's communications with China within a larger European dialogue, and in the official position of Latvia there are no surprises.

At the same time, if we look at it from a wider perspective, the year 2013 has been more than intense. The East has lived through a real dawn of self-esteem, and thus China's attitude towards the world, including towards China itself, has shown the first signs of a pattern we can call the *China Reality* (as opposite to the *China Dream*). What this *China Reality* is, and how Latvia should see itself in this brand new pattern, will be emphasised in this article.

The concept of the *China Dream* has been in use since Hu Jintao's address in 2004, and it included basically a renaissance of China internally and its emergence into global governance from an international perspective. Nevertheless, the *China Dream* remained an idealistic concept for almost decade. Indeed, 2013 was a turning point in which China's ambitions become more and more real. The reasons for this are international rather than internal.

China's outcomes from shifts in the international order

First of all, the year 2013, with its more or less clear borderline as the end of the world financial crisis, has shown which countries came out of the crisis with a raised head. And China is definitely one of them. Although there are indications of huge inner problems in China's economy – like a productivity fall and the deformed state of the balance of payments – it is not comparable with the depression in Europe and other Western countries. The main number which is used in China success stories is GDP growth – according to this number, China always follows the planned path. So, in conclusion, starting from 2013 China's attitude toward the West (especially Europe) is more self-confident than ever before.

Second, but equally important, is the role of the U.S. in Asia. The year 2013 cannot be called too successful from the perspective of U.S. foreign policy management. A partial shift of attention in the international area, and at the same time a partial inability to make sharp decisions in the case of Syria, in reality has changed the *sense of balance* in Asia – and China is keen to take the initiative. Experts on international relations, and on China especially,

have given a new name to China's mode of activity in answer to the shift of poles on a global scale – “assertive authoritarianism”.²²³ This mode of action includes two levels: national and international.

On the national level, President Xi Jinping, who took political power from Hu Jintao at the end of 2012, is proceeding on a straight course of political power consolidation. Firstly, *cleansing* along political party lines is maintained through an anti-corruption programme – particularly against those senior Chinese officials who suffer from the perception of being disloyal. Secondly, broad and varied limitations are implemented in the online environment against dissenting voices. Thirdly, but equally importantly, President Xi is institutionalising his weight in security and economic policy with the help of newly founded organisations which are under his direct control. The first of these is the Chinese equivalent to the U.S. National Security Council, which will give President Xi a direct impact on the country’s vast domestic security apparatus and its foreign security policy. The establishment of this National Security Council takes over from the Central Committee and from the Politics and Law Commission.²²⁴

The second established organisation of President Xi is an advisory and reform team, the mandate of which is to report directly to the top leadership rather than to the government. With this step, a powerful bureaucracy and its policies, which is resistant to change and nevertheless very ambitious, is balanced by the autonomy of the presidential institution. “The team will be in charge of designing reform on an overall basis, arranging and coordinating reform, pushing forward reform as a whole and supervising the implementation of reform plans,” reported Xinhua, the PRC’s news agency.²²⁵

China and the Asia Pacific region

Looking from an international perspective, the “assertive authoritarianism” of President Xi Jinping shapes the region in terms of a China-centred Asia Pacific. This also indicates a couple of activities. First is the infrastructure investment strategy – Beijing has pledged to build a significant new Asia connection facility to connect the region through railways, roads, and pipelines. This also includes the establishment of a Chinese-ASEAN maritime partnership, and enhanced regional trade and financial cooperation. Within the 10th China-ASEAN Expo and the China-ASEAN Business and Investment Summit, Prime Minister of China Li Keqiang raised five proposals on further strengthening China-ASEAN cooperation:

- 1) The creation of an upgraded version of the China-ASEAN Free Trade Area. Both sides should continue to lower tariff rates, cut non-tariff-related measures, launch dialogue for a new service trade pledge, push forward an actual opening-up to investment, strive to expand the bilateral trade volume to one trillion U.S. dollars by 2020, and increase bilateral investment by 150 billion dollars during the next eight years.

²²³ Elizabeth C. Economy, What Happened to the Asia Pivot in 2013?, Council on Foreign Relations, Online publication, 26.12.2013.

²²⁴ Malcolm Moore, China’s Third Plenum: Xi Jinping Consolidates Power, The Telegraph, 01.01.2014, <http://www.telegraph.co.uk/news/worldnews/asia/china/10444176/Chinas-Third-Plenum-Xi-Jinping-consolidates-power.html>

²²⁵ Xinhua, President Xi to Lead Overall Reform, 30.12.2013, http://news.xinhuanet.com/english/china/2013-12/30/c_133007740.htm

- 2) The maintenance of mutual connectivity in areas such as roads, railways, water transport, aviation, telecommunication and energy. China will initiate a new round of targeted loans, and give full play to the China-ASEAN Investment Cooperation Fund, to promote the building of an infrastructure-connected Asia.
- 3) The maintenance of financial cooperation.
- 4) The improvement of maritime cooperation. The Chinese side proposed setting up a “China-ASEAN maritime partnership”.
- 5) The promotion of people-to-people and cultural exchanges. The Chinese side initiated a proposal to make 2014 the “China-ASEAN Friendly Exchange Year”.²²⁶

The points mentioned above cannot be seen and evaluated separately from Beijing's expansion and the enforcement of Chinese sovereignty claims in the region. The phraseology of mutual friendship is questionable when we look at China's attitude and reactions to issues of territorial integrity. China's decision to impose an Air Defence Identification Zone (ADIZ) over a large part of the East China Sea has heightened tensions in an already volatile area. The ADIZ is the latest in a series of Chinese actions that seem to show a contradiction in the way that China engages its neighbours. The above-mentioned ASEAN example purely supports this argument – China appears to have largely succeeded in building the image of a peaceful partner in the region while swinging between the fear of an assertive giant up north and the temptation of doing business with the world's second largest economy, all at a time of growing uncertainty about U.S. reliability in this part of the world.²²⁷

The background to these events has certain heavy elements of contradiction. While in recent times President Xi Jinping and Prime Minister Li Keqiang have mounted a charm offensive in Southeast Asia, the image of Chinese goodwill in the region was discredited because of the inelegant Chinese response to Typhoon Haiyan in the Philippines. (After the Haiyan natural disaster took nearly 2,000 lives, China supported its neighbour with \$100,000 in direct aid, and another \$100,000 through the Red Cross, which is an offensive attitude even according to international standards).²²⁸ For comparison – Japan offered \$10 million in aid, even not counting the emergency relief team, and Australia has donated 9.6 million U.S. dollars.²²⁹ Taking into account this case, in which Joseph Nye's famous *soft power* concept should be followed in line with the state's ambition, it is possible to conclude that there is a contradiction in the wonderfully formed quote of James R. Holmes (professor of strategy at the U.S. Naval War College, where he specialises in U.S., Chinese

²²⁶ Premier Li Keqiang Raises Five Proposals on Further Strengthening China-ASEAN Cooperation, Press release, 03.09.2013, Ministry of Foreign Affairs of the People's Republic of China, <http://www.fmprc.gov.cn/eng/zxxx/t1073243.shtml>

²²⁷ Yo-Jung Chen, China's Contradictory Foreign Policy, *The Diplomat*, 16.12.2013, <http://thediplomat.com/2013/12/chinas-contradictory-foreign-policy/>

²²⁸ Megha Rajagopalan, China's Meager Aid to the Philippines Could Dent Its Image, *Reuters*, Beijing, 12.11.2013, <http://www.reuters.com/article/2013/11/12/us-china-philippines-aid-idUSBRE9AB0LM20131112>

²²⁹ Walter Russel, China's Disinterest in Helping Philippines Will Have Important Consequences, *The American Interest*, 12.11.2013, <http://www.the-american-interest.com/blog/2013/11/12/chinas-disinterest-in-helping-philippines-will-have-important-consequences/>

and Indian maritime strategy): “China is a uniquely benevolent great power, incapable of abusing small neighbours”.²³⁰

Of course, the ADIZ case is the clearest example of a whole spectrum of contradictions, because it leaves space for an escalation of the conflict between Japan and China. Of course, characteristics of this conflict cannot be described as *planned* or *intended* – but at the same time there remains the possibility for miscalculations and spontaneous escalations. This means that in 2014 the territorial conflict between Japan and China will be, at least, a discussible issue.²³¹ This *miscalculation option* raises a chain of rhetorical and not-so-rhetorical questions, as formulated by David M. Finkelstein, vice president of the Center for Naval Analyses and the director of the CNA’s China Studies Division in the U.S.:

- What does Beijing hope to gain by establishing an ADIZ that covers a large part of the East China Sea? The answer is simple – everything is about acknowledgment and self-esteem. It is more about signalling a presence, not looking for real solutions. Part of the guilt, of course, goes to Japan as well; nevertheless China (as it should be a *soft power* and *peace maker*), with its capital and abilities, is sacrificing potential peace on the altar of ambition.
- What is the character of China’s ADIZ and its inclusion of the Senkaku/Diaoyu islands as well as the waters off Jeju Island, which South Korea claims as its own? The Chinese government announced that the ADIZ was not aimed at any particular country – but of course Japan and the islands are at the centre of this initiative. Nevertheless, the ADIZ overlaps with the territory of South Korea as well, so the ADIZ places China's regional ambition in plain view.
- What are the possible future trajectories of territorial issues between Japan and China? And what role do you see the U.S. playing? The problem is that in this particular situation there is no clear communication mechanism on conflict resolution. Tokyo and Beijing, in fact, would not be able to deal with situation in case of some so-called miscalculation. This means that even a small spark can lead to escalation. More than this, both countries know that, but the *dawn of Asia* and raising self-esteem does not allow for effective solutions or even a way to them.²³²

It is possible to conclude that at an international and regional level China is growing not only in numbers (in terms of economics), but also in the political will to rebalance the international system, starting from the regional level. The *China Dream* to take part in global governance started becoming a reality in 2013, with a clear path towards a China-centred region. At the same time, for those who are catching the official rhetoric of China (the *peaceful development road* concept, and the concept of a *harmonic world*), it should be clear that the kind of soft power China tries to maintain is still demonised by the nature of its rising power in particular fields. Which means that the international society should be quite careful that 21st century Asia does not become a sequel to 20th century Europe.

²³⁰ James R.Holmes, Chinese Soft Power: Another Typhoon Haiyan Victim, The Diplomat, 14.11.2013, thediplomat.com/2013/11/chinese-soft-power-another-typhoon-haiyan-victim/

²³¹ Preventive Priorities Survey: 2014, Council on Foreign Relations, 26.12.2013, www.cfr.org/peace-conflict-and-human-rights/preventive-priorities-survey-2014/p32072

²³² Justin MacDonell, 5 Questions on China’s Air Defense Identification Zone, The Diplomat, 29.11.2013, thediplomat.com/2013/11/5-questions-on-chinas-air-defense-identification-zone/

China and the European Union

Knowing the international environment of Asia and the character of China, which was quite intensively expressed in 2013, it is necessary to look more narrowly to relations between China and the European Union in 2013, and then it will be possible with full speed to analyse Latvia's perspective.

Touching on relations between the EU and China, it is necessary to admit that the year 2013 is symbolic: it marks 10 years since the official *strategic partnership* between China and the EU was founded (on 30 October 2003). The establishment of the partnership came at a time of converging priorities between the EU and China, and alongside one of the worst crises in transatlantic relations, which came about mainly due to disagreements over the US-led war in Iraq and the foreign policy stance of the first Bush administration. The start of these relations was a *flying start* – the EU-15 and China adopted three initiatives (which were not followed by other distinguished *success stories*):

- 1) First, there was a declaration inaugurating the strategic partnership, which included an agreement on the joint development of Galileo, the EU-led global navigation satellite system and a potential alternative to the hitherto dominant US Global Positioning System (GPS).
- 2) Second, the same EU member states that were keen on China's participation in the Galileo project also proposed to initiate discussions on lifting the EU arms embargo imposed on China following the crackdown by the People's Liberation Army (PLA) on students in Tiananmen Square in June 1989.
- 3) Third, as bilateral trade was booming, the People's Bank of China (PBOC) made an informal commitment to further diversify its holdings of foreign currency reserves – away from the dollar and towards the euro.²³³

All these *first initiatives* characterised the main expectations of both sides – to form closely bonded economies with shared interests and common benefits. China's expectation was for more international recognition from one of the world's *soft power drivers*, while Europe's interest was in more financial investment. Ten years after 2003, much has changed, but some expectations are still there.

Europe still wants investment, but in the opinion of Beijing Europe is no longer a serious partner (in fact, if need be, it is possible not to align with Europe at all). The past 10 years of cooperation between the EU and China have been a bumpy road – and, at least at this particular moment, is progressing at two speeds. As mentioned before, after the world financial crisis the EU is not anymore a *fellow to respect*, while Europe is still desperate for investment. In fact, China, with its style of communication with Europe, is clearly showing Europe's weakest points – for instance, since the crisis of the euro, China has been establishing bilateral cooperation with the individual member states of Europe, or with regions within the European Union, while from time to time in internal rhetoric calling Europe on the whole a *crisis zone*; definitely the lack of common foreign policy of the EU is visible and indisputable.²³⁴

²³³ Nicola Casarini, The EU-China Partnership: 10 Years On, European Union Institute for Security Studies, Brief SSUE, Brussels, 35/2013.

²³⁴ Odd Arne Westad, China and Europe: Opportunities or Dangers?, International Affairs Journals, September 2013.

The year 2013 was marked by an intensification of decade long cooperation specifics between Europe and China. The European Union and China spent the first half of 2013 in a trade battle, principally over EU accusations that Chinese companies were selling approximately \$29 billion a year of solar panels into the bloc at below cost. In answer to this, China threatened to retaliate by imposing duties on EU wine. A deal on solar panels was reached at the end of July, prompting China to discuss dropping its inquiry into whether Europe was dumping wine. “We don’t want to have trade wars, we want to have trade peace,” Swedish Trade Minister Ewa Bjorling told Reuters after the Bucharest summit.²³⁵ In short, it is possible to outline the slogan of Europe as “*Investment First!*”, which is becoming more pronounced in recent years. At the same time it is important to admit that negotiations on Chinese investment possibilities in Europe haven’t seen large scale results, such as investment projects in infrastructure, production, etc. In absolute numbers we can speak more about *wannabe* investment than real Chinese money in Europe's economy. It is still more of a future plan than a present reality. But the future is always good, because it is easy to support with promises. Also, Chinese Prime Minister Li Keqiang in his first visit to post-Soviet countries within the European Union said that China wants to double trading volumes with central and eastern members of the European Union in the next five years. But this is not something new – his predecessor, Wen Jiabao, said in 2012 that China would set up a \$10 billion credit line and a \$500 million investment fund for eastern and southern Europe. There are no serious results from these initiatives at this particular moment.²³⁶

Also, EU Trade Commissioner Karel De Gucht is sceptical of China’s overtures, underlining that despite all its economic potential, Chinese forays into Eastern Europe are viewed with concern in Brussels.²³⁷ The Financial Times quoted an unnamed European diplomat as saying that the business forum in Bucharest was part of China’s strategy to *divide and conquer* Europe.

So, summing up the previous points, in relations between the EU and China there is potential, but at the same time there is a certain amount of risk. China at this particular moment seems to be more interested in *playing investor* than really *being an investor*. Of course, the incapability of Europe to act as a single actor and regain its soft power to communicate with China as equals also comes into play. Maybe both sides – the EU and China – after 2013 will focus less on hopes and promises, and more on a step by step real merging of economics.

Latvia and perceptions of China

Taking into account both perspectives – the perception of China in the international arena and the perception of China's mode of activity in relations with Europe, it is possible not only to better understand Latvia-China relations in 2013, but also to critically address the future of these relations in 2014 and beyond.

²³⁵ Philip Blenkinsop, Robin Emmott, EU Members Agree to Enter Investment Negotiations with China, Luxembourg (Reuters), 18.10.2013, www.reuters.com/assets/print?aid=USBRE99H00320131018

²³⁶ Radu Marinas, China Wants to Double Trading Volumes with Central and Eastern Members of the European Union in the Next Five Years, Reuters, 21.11.2013.

²³⁷ China Knocking at Europe’s Back Door, DW.DE, 16.10.2013.

During 2013 Latvia on average adhered to the mainstream position of the EU toward China. At all political and governmental levels the focus was on cooperation, with special attention paid to *investment discourse*. Indeed, the trade balance with China is rising in absolute numbers (exports from Latvia to China increased by approximately 80% [comparing 2012 and 2013], while imports from China to Latvia increased by approximately 9%).²³⁸ The rapid jump in export numbers is explainable by the reshaping of Latvia's economy during financial crisis and the shift in emphasis from imports to exports.

From a political perspective, communication between Latvia and China in 2013 was much more passive than in 2012. In 2012 there were official visits by Chinese government officials to Latvia, and Latvian elected officials visited Beijing. In 2013, Latvia took part in Europe's agenda toward China, but the year altogether has been quite silent. From a cultural exchange point of view, 2013 was a little bit more intensive – in the beginning of 2013 China's Press and Publication Administration, in cooperation with the embassy of the PRC in Latvia, provided the National Library of Latvia with 550 books on the history of China, its culture and society.²³⁹

Perhaps the most controversial and loudest China issue in Latvia's foreign policy arena was not even connected to China, but to Tibet. In September His Holiness the 14th Dalai Lama visited Latvia. Although the visit to all three Baltic States was informal and organised by the non-governmental sector, both in Lithuania and Estonia high level state officials arranged a meeting with Dalai Lama. Latvia's government was the exception, with the (not quite successful) excuse of not knowing of the Dalai Lama's arrival.

From narrow official foreign policy points of view, of course, it is absolutely understandable that Latvia supports China and recognises its territorial integrity, which is absolutely reasonable. There is no need *just for the sake of sport and naked criticism* to show your position. But unfortunately in this case there is the greater question of Latvia's unity with the Baltic region – its attitude toward China is in second place (because, if we value the win-lose possibilities of this particular case it is absolutely clear that Latvia *falls out* from Baltic region, which is a bigger loss than could come from the disapproval of Chinese permanent representatives in Latvia). And looking even deeper, there is the question of priorities – good, fruitful and deeply respectful relations with China is an absolute priority for Latvia, while at the same time on the everyday agenda it is an absolute priority to understand in which region a state exists and how it understands its position on the world map.

More than this, if Latvia's priority really is maintaining good relations with China, then why is 2013 so *empty* from this perspective? Why does Latvia only wait for China's investment flows, without any offers other than verbal support? And here it is important to underline that investment serves the law of economics and safe financial environments – this means that any activities in a country that show the country is falling out from its stable environment or region is a direct threat to investment. Support or denial of the Tibet question is a small page in the foreign policy yearbook, while questions of identity, stability, and self-esteem touch every issue in which there is the potential for

²³⁸ Data of Latvia-China Business Council, 24.12.2013.

²³⁹ Latvijas Republikas Ārlietu Ministrija: Latvijas un Ķīnas Tautas Republikas attiecības, 20.12.2014.

contradictions. Investment numbers from China are close to similar in all Baltic States – so losing one’s role in the region for this value is worthless.

From this perspective, Estonia, which has also had ups-and-downs in relations with China, is planning to intensify relations with China through real activities – Prime Minister of Estonia Andrus Ansip during meeting with China’s Prime Minister Li Keqiang within the Bucharest summit in November underlined Estonia’s plans to open a new embassy building in Beijing. Construction work on the building is in the final stages of completion and it is planned to be opened in the near future.²⁴⁰

The perspective of Lithuania is even more *actively radical* toward China – on 11 September 2013 President of Lithuania Dalia Grybauskaitė welcomed the Dalai Lama in Vilnius, which was absolutely exceptional because Lithuania held the presidency of the EU. There were many discussions – will China *punish* the EU as a united actor or just Lithuania for being brave enough to *keep the line* of the EU.²⁴¹ The result was a freezing of relations between China and Lithuania, but according to all signs it will be a short-term cancelation of bilateral relations lasting until the end of Lithuania’s Presidency of the EU.²⁴² EU-China level relations did not suffer from this particular case. So, at the end of the day, short-term relations between Lithuania and China are suffering, but at the same time Lithuania is even more cemented in the EU’s common policy – and because of that, the state is in a better position for communications with any foreign partners of the EU in the long term.

Conclusions and recommendations

Thus we can come out with several conclusions on the issue of how Latvia should perceive China:

- China is an absolutely recognisable and respectable actor in Asia, and 2013 is characterised by the growth of ambition of that particular actor. Latvia, if it is a true partner of China and interested in respectful relations, should support China's growth for the sake of stability in the entire Asia region. China's concepts of peaceful development, a harmonic world and the *China Dream* could serve for an international system, because they are drafted well within the huge potential of China’s soft power. Latvia should base its attitude on a simple formula – support *soft* China (which is what China wants to be according to the above-mentioned soft power concepts), and not a *threatening* China (which is a country that is respectable just because it is powerful).
- Within China’s Europe policy, Latvia should take more initiative. The year 2013 shows that relations are not too intensive –on a European level talk of investment is still only talk – and without extra effort the coming years will not bring any changes.
- In all relations with China, Latvia should definitely remember that the state is not alone on the map of Europe – more shared values with the Baltic region and the EU

²⁴⁰ Prime Minister Andrus Ansip Met with the Premier of China, Government Communication Unit, 25.11.2013, <http://valitsus.ee/en/government/76738/prime-minister-andrus-ansip-met-with-the-premier-of-china>

²⁴¹ Edward Lucas, Lithuania’s Debt to Tibet, European Voice, 19.09.2013, <http://www.europeanvoice.com/article/imported/lithuania-s-debt-to-tibet/78204.aspx>

²⁴² Vincent Metten, Lithuanian President Meeting with Dalai Lama Highlights Importance of EU Solidarity, EurActiv.com, 12.09.2013, <http://www.euractiv.com/global-europe/lithuanian-president-meeting-dal-analysis-530417>

will provide an answer on the question of how to react in controversial foreign policy issues, and will improve any relations with external actors (especially those who want to invest in Latvia). It is possible that Latvia is living through *flying years* like Europe did 10 years before, but the fact is that in any relations only proactive activity and self-understanding leads to success.

Respecting the dynamics of international relations and at the same time having self-respect is the basis for any fruitful cooperation. China, with its growing potential and impact on countries around the globe, exploits the weaknesses of those who are not prepared. Hopefully in 2014 Latvia will be more active, and at the same time more *European*, to get the best result from communications – for Latvia, and for China.

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