



September 26-28, 2013

# Conference Report

# Contents

- I. About the conference ..... 3
- II. Executive Summary..... 4
- III. The Broader Context for the New Silk Road ..... 5
  - A. Battling a Legacy of Division .....5
    - The need for a convergence ..... 5
    - Romania – the risk of being left out ..... 5
- IV. The Strategic Context for a New Silk Road ..... 7
  - A. The Syrian Question & Its Consequences.....7
  - B. Russia’s increased assertiveness and presence in the NSR Space .....8
  - C. Europe’s response to Russia and engagement in the New Silk Road ..... 10
  - D. The case for NATO engagement..... 11
- V. The Economic Context for the New Silk Road ..... 13
  - A. State actors and the economics of the NSR ..... 13
    - A space where multiple and conflicting interests meet ..... 13
    - Turkey: a regional giant’s awakening – and growing pains..... 14
    - The Middle Kingdom’s Long Reach ..... 16
  - B. The Sectors Vital to the New Silk Road and Interconnectivity ..... 16
    - A space defined by (and which can define) the energy sector ..... 17
    - The Opportunity of Infrastructure – and the lack of opportunities without it ..... 19
  - C. Convergence Through Trade – the Next Step for Unlocking Potential ..... 21
- VI. Implications for Romania ..... 23
- VII. Policy Recommendations for Romania..... 27

## I. About the conference

The second edition of the **Bucharest Forum** took place on **September 26-28, 2013**. The event was organized by the Aspen Institute Romania and GMFUS in partnership with the Government of Romania. The international gathering continued to develop the Forum's mission "to be the place where the East meets the West". The theme of this year's edition was "Anchoring the New Silk Road, Linking the Three Seas: Caspian, Black Sea and the Adriatic" and it brought together over *250 participants* from more than *20 countries*. Speakers and participants included cabinet ministers, government officials, experts, business people and media representatives from Afghanistan, Armenia, Azerbaijan, Bulgaria, China, Croatia, France, Germany, Greece, Hungary, Iran, Italy, Kazakhstan, Romania, Russia, Turkey, Turkmenistan, the US, the EU Commission, the EEAS, OECD, etc. This level of participation, engagement and coverage confirms the timeliness and importance of the topic.

The Bucharest Forum 2013 was opened with a keynote speech by Victor Ponta, the Prime Minister of Romania. The Prime Minister stressed both the importance of *a permanent, recurrent strategic and economic policy platform* like the Bucharest Forum and of *matching national and regional strategic projects* to give substance to the debate.

Conversations within the Forum covered in depth subjects related to the ***New Silk Road***, such as security and the race for energy resources, economic prospects and cooperation initiatives, transport and trade infrastructure, manufacturing, financing needs and opportunities, labor force. More than 14 dedicated panels addressed the topics proposed by organizers. The present report covers the main strategic and economic subjects.

## II. Executive Summary

The goal of the New Silk Road is twofold: strategic and economic. Although currently fragmented, the region is and can be more than the mere sum of disparate interests – be they strategic or economic. The viability of a New Silk Road relies heavily on what connects, rather than on what separates the states in the region, such as Afghanistan, Azerbaijan, Turkmenistan, Turkey or Romania, from both points of view. Individual perspectives must be harmonized and for that, understanding particular perspectives on the New Silk Road is crucial.

The overall conclusion is that the NSR's prospects depend equally on the domestic policy choices of the countries involved as well as on major international dynamics affecting the region. If this major **east-west gateway** is to be successful in creating a shared space of stability, prosperity and sustainable development, a certain convergence of the regional states' approaches is necessary.

**This requires a major regional, European and Trans-Atlantic strategic initiative.** In order to overcome existing difficulties (that should not be underestimated) *a common Western perspective vis-à-vis the NSR is needed.* This is not yet apparent but there is a momentum in this direction in both Washington and Europe.

For its part, Romania has important attributes and potential to become an integral part of a NSR initiative, but it is currently failing to achieve that potential largely due to shortcomings of its own doing, in terms of policy effectiveness and implementation.

### III. The Broader Context for the New Silk Road

#### *A. Battling a Legacy of Division*

Among the *most striking difficulties* in creating a successful NSR is the divided nature of the trade and investment space along the NSR; persistent and complex security challenges in the region or its vicinity; the reality of competing perspectives and interests; a legacy of inefficient and divisive hub-and-spoke infrastructure; overreliance on energy and commodities in trade and investment strategies; un-coordinated national development and investment strategies.

#### *The need for a convergence*

**Against the background of the US pivot to Asia, Europe needs its own rebalancing.**

Pivoting to Asia together with the US is a critical element of the West's renewed Trans-Atlantic approach. This means a central role for negotiations on the Transatlantic Trade and Investment Partnership (TTIP) and a predominant role for economic diplomacy, investments and cooperation with the region connecting Europe to Asia and the Levant.

Equally, for the countries in the three seas region - between the Adriatic, Black and Caspian Seas – this joint European-American Asian pivot creates urgent needs for convergence in order to maintain relevance by serving as the gateway for this East-West corridor. Physical, institutional and virtual infrastructures need to be interconnected, created and developed to insure this role.

The regional prerequisites for the successful implementation of such a strategic undertaking – in a complex region and less than ideal economic and fiscal context – turn around an inclusive approach and an effective use of existing opportunities. The recent changes in both Middle East's dynamics and the role of major powers were reflected throughout the three days of conversations at the BF2013.

#### *Romania – the risk of being left out*

Romania is presently not benefiting from the emerging NSR. Moreover, Romania is facing being bypassed when it comes to trans-regional infrastructure and trade routes.

To give but one example, China is building a train link along the BTC pipeline with a seamless connection to Piraeus, where a Chinese investment has tripled the container and cargo capacity. KP Cargo Logistics has launched a railway connection with China in cooperation with Far East Land Bridge and Russian Railway Logistics.

Linking this bypassing of Romania exclusively to external, regional strategic and political games is neither accurate nor useful. In fact, what needs to be addressed, on Romania's part, is the nature of the needed policy planning and project development and implementation mechanisms related to the East-West Gateway. At the same time Romania needs to be more assertive in translating some of its national interests in EU strategies and policies.

Geography is not inevitable but can be put to work. This is equally relevant to Romania, the region and its Western allies and partners.

## IV. The Strategic Context for a New Silk Road

Fluid and complex, the region's current security environment has a higher degree of unpredictability than many parts of the world. Asymmetrical threats such as terrorism and WMDs only enhance this sense of unpredictability, as do inertia regarding Cold War approaches to issues such as energy dependencies, failed states and protracted or frozen conflicts. International reactions and cooperation are the necessary ingredients of any response to these globally relevant threats.

### *A. The Syrian Question & Its Consequences*

At present, the outcome of the crisis in Syria dominates debate in the space of the New Silk Road. The resolution of this matter is not forthcoming, but its evolution stands to shape the course of future events for years, if not decades, to come.

The Syrian dossier has already served as a means for Russia to re-assert itself beyond its traditional sphere of influence. While some regard Syria as Russia's client-state, others have Russian involvement in the region is based on protecting the principle of non-intervention. Thus, Syria has enabled Russia to define the red lines, in terms of sovereignty and non-interference, which it would not allow to be crossed. So far, Russia has achieved a certain success in Syria with the Russian-American disarmament initiative, thanks mainly to the increased resilience of Assad's forces and President Obama's reluctance to intervene militarily.

Another school of thought posits that is not a WMD issue and the disarmament initiative is seen by Turkey at least as a way of buying time for the Assad regime. In this logic, this is also the reason why the initiative was accepted by Assad. Should Assad not respect the agreement, future events can determine both the region's future as well as the role of Russia and other powers here.

In the event of Syrian non-compliance, Russia can either take a step back and accept the fact that it is not as influential in the region as the USSR was, or it confront any unilateral action by the United States. With the disarmament initiative under way, the

next couple of years stand to determine the terms of engagement in the Middle East for years to come.

Beyond Syria, and thanks to the distraction created by it, the risk remains that the New Silk Road space will become a laboratory for growing extremism, posing a future problem for the EU – and not only. An area of particular concern in this regard is the energy sector, as new resources discovered in the Eastern Mediterranean could prove to be either a source of cooperation or a new source of dispute.

### ***B. Russia's increased assertiveness and presence in the NSR Space***

Traditionally, the Middle East has served as a setting for proxy wars between extra-regional powers. Throughout the Cold War, this appeared to be the case especially from the point of view of the Soviet Union, which held the Middle East in low esteem on its list of priorities. Russia's traditional interests in the region weakened further after the fall of the Soviet Union. In the run-up to the current crisis in Syria, however, changes such as a dramatic improvement in Russian-Israeli relations, an increased focus on energy and the emergence of Gazprom as an important arm of Russian foreign policy, coupled with a clear desire on behalf of Mr. Putin to recreate the "glory of the Soviet Union" have generated renewed interest from Russia in the region.

Alongside China and North Korea, Russia constitutes the end of the eastern part of the New Silk Road. As such, its role, and the roles of the other two countries and their infrastructures, constitutes a vital element of the debate regarding the Road's future, if indeed it is meant to have one.

At the same time, Russia is a country with complex and multidimensional relations with each of the other countries alongside the New Silk Road, as well as with the European Union and, most importantly perhaps, the United States. At the core of the debate about Russia's role lies the crucial question of whether the New Silk Road will bypass Russia or engage it?

The much-publicised reset between the U.S. and Russia did not bring a significant improvement in their relations. There is reason to believe that the "preset" of the relationship prevented the reset from happening. The issues that hampered the bilateral dialogue are numerous and complex. None is more contentious than the

disagreement on Iran's nuclear program, supported logistically by Russia; closely behind in terms of delicacy is the matter of Syria, with Washington condemning the use of chemical weapons and Moscow insisting on non-intervention. Human-rights issues, related to the crackdown of protests, the Magnitsky case further complicate the end goal of enhanced dialogue between the US and Russia, and between other Western countries and Russia.

However, notwithstanding the Syrian crisis, Russia appears to be searching to define its role in the Middle East as part of a broader quest for its national identity. Russia is leading a customs union, including Kazakhstan, Belarus and Armenia, which has only recently announced its decision to join the initiative and could be interpreted as going through a political shift. Russia's Eurasian Union is a showpiece example in this regard, and it offers an attractive alternative to the EU's Association Agreements and Deep and Comprehensive Free Trade Agreements (DCFTA). While some might view the EU's offers as more attractive, Russia's is not unappealing. The Eurasian Union can offer some countries rather attractive economic opportunities, particularly when considered in the context of the possibility to avoid the discourse about democratic values in politics and society. The reality remains, however, Russia has more work to do in order to modernize and make itself a more attractive trade and investment partner to its neighbors.

Through a switch of focus away from the EU, and towards China and central Asia, Russia appears keen to signal its own "pivot", as shown by Vladimir Putin's frequent visits to the Far East, and by China's rise to being a top trade partner to Russia, displacing Germany. On this note, it has to be mentioned that whereas Europe sees China as a threat, Russia sees it as an opportunity. Be that as it may, however, it does not signify that Russia will leave Europe aside, or disengage from it altogether. The EU remains of utmost significance to the Russian economy, and the energy link between Russia and Europe is at best looser, but still very much in existence and a source of interdependence and a reason to cooperate.

Still, it can be expected that increased economic strength, if materialized, and policy shifts away from the EU, will lead to more aggressive tactics on Russia's part.

In the 2008 war in Georgia, Russia demonstrated its determination to increase its influence in this region, even at the cost of shaking up the political landscape in a rather overt manner. Russia's strategic approach has been clearly defined, and so far it has had no match from the EU. While Russia has appeared less than shy in its willingness to use military power, European countries have yet to move away from their reluctance to consider it.

### ***C. Europe's response to Russia and engagement in the New Silk Road***

At the same time, the EU has deployed noteworthy „soft power“ instruments in support of fostering the effort political stability and increase economic interconnectedness within Eurasia, against a backdrop of the US pivot away from Europe and closer to Asia. The Eastern Partnership, for instance, aims to promote better governance and cooperation between societies on a wide range of dossiers, from sensitive issues such as security to more practical ones such waste water management. Also, Association Agreements could be viewed as do-it-yourself tools that can help countries increase their trade, based on the idea that access to their markets should be driven also by the needs and expectations of trading partners and not just geopolitics.

Nevertheless, it has to be accepted that the recent financial crisis and the sovereign-debt crisis in the EU have taken focus away from longer term strategic priorities. However, it is becoming apparent that particularly in the countries most affected by the crisis, there is renewed recognition of the potential benefits arising from a more comprehensive economic and political integration with the East.

The necessity for Europe to further integrate its economy with that of Central and South Asia has been placed in sharp relief by recent trends in the global economy, and nowhere is this more apparent than the energy sector, where the diversification of energy links can reduce dependency on a single supplier.

There are three possible pillars for the EU's regional energy strategy: promote the development of new energy resources, secure energy supplies in the region and the creation of new routes that will help Caspian resources reach Europe and the East. In

light of these, the EU needs to fully appreciate the strategic importance of opening the southern corridor through the TANAP and TAP pipelines.

As it examines its strategic options and initiatives in the Eurasian region, the EU needs to be aware of the twin-track transition that affects countries in the area. On a macro level, the shift away from a Western-dominated narrative is apparent, as is the attractiveness of a so-called new order or model of socio-economic governance. On a regional level, homegrown organizations and local actors become more important, and the EU's response has been to increase its interaction with ASEAN.

#### ***D. The case for NATO engagement***

*Economic prosperity is strictly connected to security.* Today, the region's security is facing complex threats: terrorism, trans-border crimes, energy interdependence, failed states, frozen conflicts or unpredictability of certain actors are such threats. On a more practical level, the challenges the transatlantic and Eurasian communities face in their efforts to provide stability in the region include: 1) the limits of keeping the US engaged in the region - the budget cuts impact significantly US's ability to deploy its forces throughout the region; 2) the asymmetric (less military) threats against Europe/EU; 3) Russia's inwards focus - Russia is focusing more and more on its immediate vicinities ; 4) Iran; 5) NATO's frail connectivity with other partners that would enable them to react to emerging threats in an organized way; 6) crisis management; and 7) economic threats - which could be tackled by trade and investment negotiations between EU and US, US and Asia, and EU and Asia.

NATO's role in the New Silk Road region has been defined by the Afghanistan mission, which was seen as an abandonment of euro-centrism. The prospect of the end of the Afghanistan mission, a smaller US defence budget combined with the much-discussed pivot to Asia raises the question of the extent of NATO involvement in the area, versus a retreat to its euro-centric roots. At present, the promise of membership made to Georgia is the most concrete, but also the only, premise for ongoing engagement by NATO in the region.

Luckily, NATO has arrange of tools at its disposal that it can deploy in order to have a positive effect on its neighbouring areas. Enhancing partnerships in Asia and a revamped

approach to the Partnership for Peace programme are but two ways in which the alliance can retain a global outlook. This could serve the current context better, recognizing that countries in north Africa and the Gulf have different agendas from the CEE countries which, not too long ago, were keen candidates to join the organization.

In light of the constraints outlined above, NATO could find new and innovative ways to deepen its engagement via public-private partnerships and by expertise from the scientific community. While the importance of traditional military actors cannot be discounted, their role needs to be better defined. Alongside them, think tanks and civil society in general can play a very important role in defining the purposes of the Silk Road.

## V. The Economic Context for the New Silk Road

The New Silk Road initiative is seen as offering business opportunities for the Western world by means of fostering competition and allowing room for economic clusters to develop. Free competition and removal of trade barriers are advocated for, as a basis for the future development of the region. The negotiations between the US and the EU on trade are also highly anticipated by the US business world, as a precursor to opportunities in the EU's near-abroad.

The benefits of a New Silk Road would be manifold, by creating the possibility for new infrastructure projects, while removing bureaucratic hurdles, and helping to erase old prejudices and outdated trade policies. The new Silk Road's ultimate result can and should be increased connectivity and business opportunities for both for the West and the region.

There are complex issues that need to be addressed in the political relationship between the EU and Eurasian countries, and recent years have proven that old habits die hard.

### *A. State actors and the economics of the NSR*

#### *A space where multiple and conflicting interests meet*

Large economies like the EU, the US, China, Russia and Turkey have conflicting strategic and economic interests in the region and employ, with various degrees of efficiency, different instruments to meet their goals. The EU and the US tend to promote their strategic interests by advocating the opportunities that the New Silk Road initiative would bring to smaller but rich in resources economies in the region, without significantly pushing forward for it, technically and economically. Russia is pursuing a more active approach of growing influence in the region, building on existing cultural and economic backgrounds with such smaller economies. China needs resources to maintain its development pace and is also more interested in developing bilateral cooperation in the region.

### *Turkey: a regional giant's awakening – and growing pains*

Turkey has similar reasons and is actively seeing not to be bypassed by potential major economic projects. Turkey sees itself as an anchor to a New Silk Road, relying mainly on energy transport infrastructure from East to West.

Cooperation between energy resources rich countries in the region with their potential Western consumers is essential. Thus Turkey is an advocate of regional cooperation in trade and infrastructure, as it would benefit its exports by reducing transport costs. Improved security in the region would also facilitate trade by reducing insurance costs.

Turkey can be instrumental in making the New Silk Road by continuing with its emerging approach of engaging virtually all partners to open up to trade and bi- and multilateral cooperation. Rooted in the conviction that its position on the map makes it a natural, if not even indispensable, hub for the region, Turkey's approach poses both advantages and risks.

Already, its foreign policy is currently over-stretched in the Middle-East, suffering from evident deficits in delivery, which undermines the credibility and potential for it to have influence and leverage not only in the South and the East, but also with Russia, in the Balkans and the Caucasus.

Turkey's own "pivot" towards the Middle East, including the involvement in hot conflicts justified by loss of Turkish life in Syria, appears to stem from a perceived snub by the European Union. The EU's importance in promoting democracy and the rule of law has suffered a credibility loss in Turkey due to the Union's continued inability to display a coherent approach to this very idiosyncratic candidate for membership. While feeling at times snubbed by the EU and at other times patronized by it, Turkey appears not to have allowed this to prevent it from pursuing strategic and selective engagements with member-states such as Romania, where Turkey is a major investor in the transportation and logistics industries. More broadly, Turkey's need for technology exchanges make cooperation with the EU a must for the longer run.

Major infrastructure projects such as the TANAP pipeline further cement Turkey's key role as a gateway between the East and West. This, alongside the sheer scale of its economy and the evident advantages of its position, reinforce the argument that all major economic projects in the Levant region and in the Three Seas region should pass through Turkey.

Notwithstanding all the advantages that Turkey's position and policies bring, its trade deficit, stemming from a dependence on imports, comes with vulnerabilities. These were brought into sharp contrast by the Turkish financial crisis of the early 2000's highlighted a lack of capital and a need of foreign direct investment. Additionally, in 2009 Turkey's economy registered its largest decline, and its overreliance on FDI surfaced.

Turkey's geographical placement offers it an important strategic role as a transit country for gas supplies from the Caucasus to the EU. However, politics that the EU can find common ground with need to accompany Turkey's geostrategic advantages. If Turkey remains committed to implement the necessary reforms in order to join the EU, even if lacks a guarantee that it will be a member of organization anytime soon, this will signal there is political will in Turkey to have a government that functions within the bounds of democracy.

Turkey's privileged status as a transit country was evidenced in 2011, when an agreement has been reached to build the TANAP pipeline that will cross Turkey from the east to the west, where it will be connected with Trans Adriatic pipeline.

Other economic cooperation initiatives in the Western world, such as the Transatlantic Trade and Investment Partnership (TTIP), also influence the way the regional actors position themselves in protecting their national interest. TTIP may cause a loss of 20 billion dollars, nearly 2.5% of Turkey's GDP in the long term, unless a free-trade agreement is signed by Ankara with the US. From this perspective, the new Silk Road initiative is a better option for Turkey, unless it is aligned with TTIP.

## *The Middle Kingdom's Long Reach*

China is seeking trade relations with the US and the EU, it is also in the process of solidifying relations with countries in the region and its influence should not be overlooked. Beijing has recently proposed forming a Silk Road economic belt with 5 central Asian states: Kazakhstan, Turkmenistan, Uzbekistan, Kyrgyzstan and Tajikistan. Another major player in the region, Russia, is also seeking a role in the formation of the New Silk Road. Russia is leading a customs union, the Eurasian Union, including Kazakhstan, Belarus and Armenia, which has only recently announced its decision to join the initiative and could be interpreted as going through a political shift.

### ***B. The Sectors Vital to the New Silk Road and Interconnectivity***

In the logic of post 2014 security in Central Asia, the New Silk Road initiative could be used to further promote interconnectivity in the region and to enlarge the market for Afghan resources (mining). However, certain security, financing and sustainability challenges have to be addressed first. These need to be part of the post 2014 logic.

The New Silk Road Region exhibits a number of dissimilarities in terms of religion, political models and geography, all of which make cooperation more challenging. One of the main challenges is the lack of an organization that could help the advancement of reforms.

The countries of Central and Eastern Europe have benefited from the reforms they had to implement in order to become member of the EU and NATO. In contrast, although there are a few Eurasian supranational organizations, such as Commonwealth of Independent States or The Shanghai Cooperation Organization, there is a need to consider a framework to constructively integrate these nations.

Economic stability could be the driving force behind the political future of the New Silk Road region. Business can help overcome some rifts that are present between countries, thanks to the fact that the criteria for investing have not changed, with investors eyeing countries that have political and economical stability, competent commercial judges, rule of law, transparent government actions and an educated workforce. These criteria have become global requirements that have a much lesser

ideological stigma attached to them – after having been promoted by the West, now they are de facto hygiene rules for business and investment.

### *A space defined by (and which can define) the energy sector*

One cannot imagine economic development in the absence of access to energy resources. The EU and China – as two major consumers of oil and gas, are competing for Central Asian energy resources in their efforts to diversify their suppliers. The dimensions of Europe's energy challenge are on par with its status as the world's largest trading bloc. It imports more energy than any other consumer, and 70% of it is natural gas. Furthermore, its situation is compounded by supplier concentration and the excessive reliance on Russian gas. For instance, Russian gas accounts for 90% of supply in the Czech Republic and Bulgaria, while in Ukraine, Hungary and Romania it's around 23%. Reliance on a single supplier puts the consumers at risk in the event of disruptions in the supply chain. These may be caused by potential problems in transit countries, or by unilateral policy and price decisions by the producing countries, as was seen in 2007 and 2008.

Supply diversification in the EU is rendered more difficult by the depletion of existing resources, public opposition to the usage of hydraulic fracturing (fracking) needed to exploit new gas resources, the phasing out of nuclear power in countries like France and Germany. Globally, the emergence of the energy hungry economies of India and China has tilted the balance of power towards producers aware that they have abundant demand to sell their output to.

In May 2013, recognizing the importance of energy security, the European Council moved the issue to the top of the EU agenda. More particularly, it aims to ensure the energy security of EU households and to provide competitive prices for EU companies. The supply routes for gas are a crucial factor in this equation. Access to the output of the EU's several gas rich neighbors has been delayed as the construction of the Southern Corridor has stalled for the past 15 years, due to the volatile political situation that engulfs the countries South Caucasus and Central Asia.

As an alternative to supply from its neighbours, the EU could bolster its energy security thanks to the shale gas revolution taking place in the US, and which has transformed the US into the world's largest producer of gas. If the Washington administration approves export quotas, NATO countries could benefit. In turn, such a development could also speed up the development of terminals in Croatia and Poland.

However enticing the prospect of US gas supplies might be, there is no getting away from the reality that the Caucasus offers the EU a better long-term solution for diversifying its energy supply. The countries of the region exhibit variety in terms of their ability and willingness to become energy partners to the EU and rest of the world.

Azerbaijan wants to contribute to the development of trade with Southern Europe and Central Asia. The energy sector can and should spearhead such efforts, and Azerbaijan has the resources and the political will to export them to Europe. In addition, its geographic position allows it to be a regional transit hub for the Trans Caspian supplies from Turkmenistan and Kazakhstan. SOCAR, the Azeri state energy company, is developing a number of projects that have the potential to become the cornerstone of Europe's energy security, as is the case with the AGRI that promises to deliver natural gas to Romania and Central Europe.

Turkmenistan has the 4<sup>th</sup> largest gas resources in the world, but the lack of a business environment and favorable political context has hampered the development of gas exploitation. Lastly, Kazakhstan can become a major player in the oil market. In the meantime, however, Kazakhstan, for example, has made important investments in its infrastructure. A new rail corridor is being developed in order to reduce shipping times along with a new route from the North to the South, connecting Kazakhstan to Russia, Iran and Turkmenistan. The goal for Kazakhstan is to reach 50 million tons of freight passing through the country by 2020. The business community of Kazakhstan is divided on the benefits of being part of the Eurasian Customs Union, because of unfair economic gains. In this sense, it is becoming more important for Kazakhstan to remove all trade barriers with the Europe.

For its part, Iraq could provide 15 million cubic meters of gas to Europe, but the central government in Baghdad cannot reach an agreement with the Autonomous Region of Kurdistan over revenue share.

### *The Opportunity of Infrastructure – and the lack of opportunities without it*

The energy sector has the potential to be the main driver behind opening the New Silk Road. However, opportunities abound well beyond this sector, however vital it might be in and of itself. Several barriers stand in the way of achieving the next stage of cooperation in this area. These barriers include a lack of knowledge, of legislation, of communication, of trust, and also of international political influence on the part of actors in the Three Seas region.

The interconnectivity and interoperability of physical and virtual infrastructure would foster trade. Currently, however, transport and trade infrastructure is fragmented in the region. A consistent strategic approach towards its development is in order, but with a more pragmatic tactical approach, of building on existing bilateral/ multilateral cooperation relations and pursuing more immediate goals such as increasing connectivity and ensuring interoperability.

The development of interregional transport and logistics infrastructure, in the logic of the existing European corridors such as TRACECA, by smaller, critical steps, looks promising if the right approach is adopted by the involved governments. Rail and intermodal transport infrastructure were identified by the panelists as investment priorities, as well as river transport infrastructure, in the case of Romania (the Constanța-Rotterdam corridor).

Financing sources are available for the development of the European infrastructure segments but the actual absorption is low, especially in the case of Romania. In the region, countries also compete for financing made available by international development banks. In the absence of credible projects, private finance sources are scarce, either.

The New Silk Road region is currently not exploiting the significant potential to be an entry gate towards the EU from the Far East, as well as and a trade and logistics hub in the south of Europe. Sea-borne trade levels are currently well below their potential levels in southeastern Europe, even though routes to and from the Far East are shorter from here than from western ports.

To unlock this potential, a study by PwC identified the aspects that investors find the most important: location, a high-quality infrastructure, availability of optimal transport solutions, competitive business and fiscal climates, stable and predictable laws. Participants in the study put forth some long-term measures for achieving the region's hub potential: a coherent investment strategy for infrastructure development, in-land Danube ports and developing a multi-modal transport strategy. Short-term measures proposed for increasing trade include: VAT exemption for all imports; the reduction of registration costs or reporting requirements for logistics.

While it is recognized that financing is always an issue in the context of regional strategies and large infrastructure projects, participants have said that in addition to EU funds, public-private partnerships could be a valuable vehicle for helping bring initiatives to fruition. Furthermore, in view of the fact that transport via the Danube would reduce carbon emissions; special environmental funds can be attracted to support this development.

The success of the Ancient Silk Road was based on the interconnectivity between the cities. More importantly, everybody respected the rules of trading in the Silk Road Region. Today, challenges in the development of the New Silk Road may find an answer in creating an infrastructure network that ensures interconnectivity and allows for interoperability, including the harmonization of legislation, fast express ways and better border crossing conditions. One feasible approach would be to concentrate on developing smaller hubs or nodes that connect distant points on the map, such as, Turkmenbashi, Aktau, Poti, Constanța or Istanbul.

If communication was important for the ancient Silk Road it remains crucial for the NSR. This holds true, especially in a rapidly changing technological environment. Investments in virtual infrastructure will allow for rapid exchange of information at reduced costs,

provide a medium for education services and will enable the shaping of common values, the harmonization of potentially diverging interests which, in turn, support trade in more secure conditions. Romania is currently involved in the development of virtual education programs and sees its virtual infrastructure building capabilities as a strength for its involvement in the New Silk Road.

Physical infrastructures are equally conditionality for the success of the NSR. Creating the basis for **an East-West Gateway** requires a series of policy and investment decisions. These are to be taken in a relatively narrow window of opportunity. They concern both existing and new infrastructures first related to facilitating trade: ports, railroad, multi-modal transfer facilities, and logistics hubs. Constanța's port and the Danube can play a major role in accessing Eurasia, and shortening the transport routes from China to Europe and back. Developing this in convergence with other major investments in the three seas are between the Adriatic, Black, and Caspian Sea is part of the western anchoring of the New Silk Road.

### ***C. Convergence Through Trade – the Next Step for Unlocking Potential***

Another key dimension for the western anchoring of the NSR concerns trade. Ongoing trade negotiations will shape the context as much as security developments are shaping it today. From both a strategic perspective as well as a practical one, the EU-USA Transatlantic Trade and Investment Partnership negotiations can be considered a driving force for all other trade talks.

The Transatlantic Trade and Investment Partnership (TTIP) is a trade agreement that is presently being negotiated between the European Union and the United States. It aims at removing trade barriers in a wide range of economic sectors to make it easier to buy and sell goods and services between the EU and the US. It also aims to tackle barriers behind the customs border – such as differences in technical regulations, standards and approval procedures.

The TTIP negotiations will also look at opening both markets for services, investment, and public procurement. They could also shape global rules on trade.

The challenges are huge, as the relationship between the parties is complex, with high economic and political stakes involved. In addition, various other players, including those situated along the New Silk Road, will likely be affected.

TTIP may cause a loss of 20 billion dollars, nearly 2.5% of Turkey's GDP on long term, unless a free-trade agreement is signed by Ankara with the US. From this perspective, the new Silk Road initiative is a better option for Turkey, unless it is aligned with TTIP.

China is seeking trade relations with the US and the EU, it is also in the process of solidifying relations with countries in the region and its influence should not be overlooked. Beijing has recently proposed forming a Silk Road economic belt with 5 central Asian states: Kazakhstan, Turkmenistan, Uzbekistan, Kyrgyzstan and Tajikistan.

TTIP is just a part of a global strategy, as the Black Sea-Caspian Sea corridor would be the natural link between the Euro-Atlantic space and Central Asia. Romania being situated at the Eastern border of the EU could take advantage of its geographic position in turning itself from a periphery economy into a pivotal one. The added value of such a corridor is in terms of transportation, energy, investment, as well as military. Moreover, in the framework of the New Silk Road, Romania favors the development of river transport routes in Europe with Constanța being at one end of the trading route and Rotterdam at the other.

## VI. Implications for Romania

There is a set of specific difficulties hindering Romania's contribution to the NSR. These are brought about by both structural and circumstantial conditions related to internal and external challenges.

External difficulties to Romania's positioning and benefiting from an emerging NSR are linked to its lack of ambition that becomes evident in its "encircling".

China is building a train link along the BTC pipeline with a seamless connection to Piraeus where a Chinese investment has tripled the container and cargo capacity. KP Cargo Logistics has launched a railway connection with China in cooperation with Far East Land Bridge and Russian Railway Logistics. With the choice of TANAP and TAP for Azerbaijani gas and the sidelining of NABUCCO West as the Southern Gas Corridor

Linking this encircling exclusively to regional strategic and political games is neither accurate nor useful. In fact what needs to be addressed is the nature of the policy planning and project development and implementation mechanism. At the same time Romania needs to be more active in translating some of its national interests in EU strategies and policies.

The major internal challenges are governance and project implementation issues; the difficulty in establishing a clear purpose and lasting set of projects; these are compounded by structural issues, financing and skills shortages etc.

After four years of economic struggle and severe austerity measures implemented, Romanian economy seems to have been turned back on the positive track. Development potential is present but further actions are needed in order to materialize it, to foster economic growth and to actively contribute to the creation of the New Silk Road. In turn this can serve as a major policy focus and private sector investment target.

What is needed for Romania to economically move forward? More efforts are needed on predictability of public policies, anti-corruption measures, administrative – including tax – simplification, investment promotion such as one stop shops or investment promotion agencies, support policies for SMEs which are very important because they

can push the economy forward and last but not least innovation and skills. *What is paramount is a clarity of purpose.*

In Romania's case, the EU orientation and adoption of necessary standards has been the paramount priority of recent years. Dealing with the shortcomings of the economic crisis also occupied significant public policy space. New opportunities of development such as the New Silk Road impose new challenges and require more weight to be added to policy measures sustaining growth. Two major priorities are considered: financing and skills.

Financing for economic stability can be obtained in many ways: by increasing the EU funds absorption, promoting exports, employing public investments and increasing the state guarantees level for the stimulation of aggregate demand. Setting clear priorities for the limited resources available from the state budget and reimbursable funds and multi-annual budgeting are preconditions for efficient public investments.

Romania is one of the potential key players in the region's energy sector, thanks to vast resources in both conventional and renewable energy. Indeed, Romania's energy assets put it in a pole position to become the energy hub of Europe. Before Romania can fulfill its potential, however, a number of problems that need to be addressed, both internally and in the broader context of the EU's effort to enhance its energy security.

Investment in the energetic infrastructure that could foster the necessary interconnection with Serbia, Hungary, Moldova and Bulgaria have not yet materialized. A further predicament blighting Romania's energy strategy is the slow pace of modernization of Romania's main power plants. For example, the building of the Tarnița Lăpustești hydroelectric power plant, which is meant to bring the Romanian energy system into balance, has not started because of the lack of investors. In addition, the slow pace of negotiations is slowing the development of Romania's nuclear energy reactors, whilst the modernization of the coal driven power plants has been lagging for the past 10 years.

Despite these challenges, Romania's energetic security is ranked 9<sup>th</sup> globally, according to a report published by World Energy Council.

In the near future, this can be improved by exploiting the gas resources of the Black Sea, which can assure the country's energy independence, and could turn Romania into an energy exporting country by 2018-2020. Also, the country intends to develop the Ofcom energy exchange and open the possibility to starting a gas exchange. Foreign investment can be attracted by selling the equity stakes in Romanian energy companies such as Transgaz, Romgaz and Nuclearelectrica. At the same time, Romania will continue to develop its relationship with energy rich Kazakhstan, Azerbaijan, Turkmenistan and Uzbekistan.

Infrastructure concerns beyond the energy sector are also near the top of the list of Romania's challenges. The modernization of Romania's road infrastructure is lagging behind that of its neighbors. Romania should concentrate on small infrastructure projects in critical nodes of its infrastructure network and which allow for inter-modal transport services, using a balanced mix of finance instruments such as the available EU funds, PPPs and strategically on promoting its interests in bilateral/ multilateral, regional relations.

A major obstacle in the way of growth is the current state of private credit. There is no long-term growth without restored confidence in private credit. Foreign direct investment is at low levels and banks operating in Romania do not seem to have recovered confidence. The quality of the business environment may be part of the explanation. Another part of the explanation may rest in the fact that what Romanian economy actually lacks is equity and, to a lesser extent, bank loans. The development of the local capital market could be nurtured by increasing the pace of the privatization of state owned economic operators. A local capital market is, as always, seen as an important factor in investment. In more mature markets, one can see that capital markets cover up to 50% and, in some cases, even 90% of the financing needs of the private sector. Romania, on the other hand, is at about 98% level of bank financing and this is in no way a sustainable situation. Increasing the pace of privatization of the state owned economic operators and the disputable fostering of the local financial market deregulation were among the proposed solutions.

The development of human capital is another target to be envisaged, the main goal being the improvement of the labor force skills. New technologies require skilled

workforce. Increasing the level of competences is also essential because unskilled workers are vulnerable workers. Financing is crucial for the process. Apart from upgrading its workforce's skills, Romania faces today another important challenge: that of raising employment rates. Increasing employment will boost growth by bringing more people to the production sector and upgrading worker skills will mean they are more productive and employable. Today, Romania has a 60% rate of labor market participation. Raising employment has been hindered by the fact that labor costs have been increasing faster than productivity. Productivity growth should be tracked.

Another major obstacle in the way of growth is the inefficiency of policy implementation regarding large-scale projects. This can be quickly addressed via priority areas. The potential for the NSR to serve as a policy focus and convergence creating force is evident. An authentic case for public private partnership this should be considered as a key short term priority. Establishing the country as a **Gateway on the East-West Corridor** is not only a condition for a successful participation in a NSR but also a condition for the sustainable development of Romania as an EU member state, NATO ally and a successful society.

## VII. Policy Recommendations for Romania

Based on the preliminary analysis of the results of the Bucharest Forum, **Romania's successful participation in a NSR trade and manufacturing agenda** implies the following:

1. Making a key governmental priority in establishing Romania as a player on the East-West trade and investment Corridor
2. Drafting and promoting at EU level the set of policy positions that are needed for a joint US-EU pivot to Asia
3. Making the East-West Gateway project as a major strategic P&P undertaking; Creating a public-private project team for its delivery
4. Establishing the internal conditions for the public and private investments needed by making Constanța and the Romanian part of the Danube as an East-West Gateway for the NSR
5. Facilitating the regional community required to support a convergent regional approach to the western anchoring of the NSR
6. Actively engaging government and business partners at the east of the Black And Caspian Seas with a view of increasing the number and relevance of joint projects
7. Matching the policy options for its NSR participation as an East-West Gateway with its set of growth and employment strategy for national development; prioritizing public spending (investment) in interconnecting infrastructure with a clear priority for bridging and bottle neck reduction projects.