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PRESS RELEASE

A JOINT RESEARCH ON TRANSITION, INTEGRATION AND RESTRUCTURING IN THE NMS AND NIS: ADDITIONAL PAPERS NOW AVAILABLE

INDEUNIS, an international research project coordinated by wiiw and financed by the European Commission from the 6th Framework Programme, brings together ten research institutes from *Austria, Poland, Hungary, Estonia, Finland, Russia, Belarus, Kazakhstan* and *Ukraine* which jointly investigate the recent experience with economic transition, industrial restructuring and integration in both the New EU Member States from Central and Eastern Europe (NMS) and selected Newly Independent States (NIS: Russia, Ukraine, Belarus, Kazakhstan and Moldova).[1] In March 2006 some 19 papers from the initial stage of the INDEUNIS project ('Industrial Restructuring in the NIS: experience of and lessons from the new EU Member States') were published – see wiiw's website at www.wiiw.ac.at > Research networks > INDEUNIS. The latest INDEUNIS papers analyse the patterns of structural change and integration on EU-NIS borders as well as the challenges of EU enlargement and WTO accession. Besides, a number of case studies on restructuring experiences in Moldova, Kazakhstan and the Baltic Sea region, as well as on the development prospects of the automotive industry in Russia, is also available on the project website.

Research by the *Vienna Institute for International Economic Studies – wiiw (Austria)* analyses the trade integration between the enlarged EU and the NIS, in particular the evolution of regional and commodity trade composition. A detailed market share analysis reveals the emerging specialization patterns. The recent developments indicate closer trade integration among the NMS, a declining trade integration among the NIS, as well contradictory shifts in the NMS-NIS exports and imports. The importance of the NIS as export markets for the NMS is growing, in particular for the NIS neighbours. The key NMS manufacturing export commodities are chemicals, machinery & equipments, motor vehicles and food products whereas NMS manufacturing imports from the NIS concentrate on a couple of basic manufactures such as basic metals, refined petroleum, chemicals and fabricated metal products. Wide-ranging modernization and industrial restructuring in the NMS has been facilitated by the process of EU integration and massive inflows of FDI whereas the resource specialization of the NIS generally increased as reforms and restructuring were delayed. Trade integration in the Baltic Sea Region was investigated by the *Institute of Baltic Studies – IBS (Estonia)*. The authors find that the competitiveness of industry in Estonia, Latvia, Lithuania and Poland is still lagging behind. An equalization of export prices has predominantly taken place in the trade with raw materials. In trade with the majority of manufactured goods there are deficits as these economies continue to act as lower value-added parts of the cross-border clusters in the whole Baltic Sea region.

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[1] Apart from individual research papers, the INDEUNIS website provides a detailed description of the entire project, its individual work packages as well as contact addresses of the participants.

The accession to the EU has brought about changes in the NMS trade regimes. Their effects are explored in the paper prepared by the *Foreign Trade Research Institute – IKCHZ (Poland)* by the example of Poland's trade with its eastern neighbours, Russia and Ukraine. The study concentrates on the effects of the adoption of the Common External Tariff (CET) and the EU's preferences for imports from Russia and Ukraine. The CET effects on trade in industrial products have been limited since the increase in duties affected only 5% of Russian and 9% of Ukrainian exports to Poland. The adoption of EU trade defence instruments had a greater impact, in particular on Polish imports of steel (first of all from Ukraine) and fertilizers (mostly from Russia). Nevertheless, other factors, largely unrelated to EU accession, have had a stronger impact on Polish trade with Russia and Ukraine. The non-registered transborder trade turnover, also in relation to Poland's eastern neighbours, has been growing during the transition period. The peak was reached in the period 1992-1998, yet the Russian crisis adversely affected many small Polish businesses. The recovery observed after 2000 was temporary as conditions deteriorated during Poland's integration with the EU. The value of the registered trade of Poland's eastern voivodships with their neighbours is small and the commodity structure very unstable. The development of trade is hampered by the small absorptive capacity of the regional markets, by the low competitiveness of manufactured goods as well as by the limited amount of goods and services offered for exports. The involvement of foreign investors in these regions is limited. Border regions suffer from shortage of capital resources and thus do not foster modernization and competitiveness. The example of Kaliningrad illustrates the barriers that limit the development of transborder cooperation. These include differences in the administrative systems, in particular the low degree of independence of local authorities, a weak infrastructure, the visa regime, unstable law and limitations for investments in Russia. Poland's economic cooperation with the Kaliningrad District is mostly perceived as a vehicle to enter the enormous Russian market.

The economic development and industrial restructuring in regions that border on the EU has been more rapid than in other Russian border areas. The paper by the *Institute of Economy, Russian Academy of Sciences – IE RAS (Russia)* shows that among the factors contributing to this discrepancy are the more developed institutions that support economic cooperation between Russia and the EU. The paper argues that a simultaneous strengthening of cross-border cooperation and the development of the neighbouring regions' economies would have positive implications for Russia's global political and economic role. Still, Russia is concerned about the enlargement of the EU and its multifaceted and controversial impact on economic transition and industrial restructuring processes. The comprehensive analysis of these issues undertaken by IE RAS argues that Russia is trying to foster its specific vision of the European integration based on two pillars: the European Union in the West and Russia-initiated integration models in the East. In this way Russia could retain its political and economic influence on the post-Soviet European space whereas the EU's Neighbourhood Policy (ENP) is viewed with suspicion. The conflict of interests between the EU and Russia is increasingly apparent: the mutual economic relations are characterized by ambiguity and competition which negatively affect the efficiency of this collaboration.

The Russian concept of regional integration (the Common Economic Space, CES, between Russia, Ukraine, Belarus and Kazakhstan) is analysed in another paper by IE RAS. The originally designed concept is not viable while the sole creation of a free economic zone is appealing to Ukraine only. Nevertheless, the basic CES idea is supported by the business community. This integration project should be viewed as a 'bridge' between the EU and the CIS, and as a part of the evolving Common European Economic Space between the EU and Russia. This form of cooperation could serve as a consolidation factor on the post-Soviet space, and secure a combination of the two major directions in Russian foreign economic policy, i.e. the cooperation with both the CIS countries and the EU. This meets also the interests of the ‘problematic’ party to CES Agreement, i.e. Ukraine, as it is consistent with the latter’s priority strategy of European integration.

The effects of EU enlargement and WTO accession on Russia were investigated also by the *Development Centre – DC RF (Russia)*. Their paper shows that in the short run there was a modest increase in Russian energy exports to the NMS, mirrored by a more significant rise of finished goods imports from the NMS to Russia. The potentially negative impact on Russian agricultural and machinery exports would be lower than a possible decline in energy exports. The survey among Russian managers revealed organizational, economic and political factors that impede an increase in EU-Russian trade, and the attitudes towards WTO accession. Enterprises already involved in foreign trade stress deficiencies in Russian economic policies, such as the complex taxation, low quality of output and the lack of information on commercial legislation in the EU as impediments. Enterprises that operate only on the domestic market mention the low product quality and a poor knowledge of EU legislation as drawbacks. The opinions regarding WTO accession are split, but those who are in favor slightly prevail. One of the main factors that shape the negative attitudes towards WTO are fears of foreign competition. However, such attitudes are shaped by the situation in the enterprises themselves rather than by the potential increase of competitive pressures. The attitudes regarding the financial implications of WTO accession are unclear, though generally those companies that are already exposed to foreign markets are not afraid of WTO accession; they expect an increase in foreign investments and approve the arrival of foreign banks and other financial institutions. The position of domestically oriented enterprises is uncertain and highly sceptical.

Indeed, the negotiations on Russia’s accession to WTO have been dragging on for one and a half decades. A paper by IE RAS (Russia) reviews in detail the negotiation results as of mid-2006, the key terms of accession, as well as systemic problems such as the conformity of Russian economic and trade policies with WTO rules. The authors conclude that Russia’s WTO accession would represent a step ahead in the complicated and controversial recovery in the new historical and economic circumstances, consolidating a proper place of Russia in the global economy by securing fair and mutually beneficial trade relations.

The EU enlargement brought about some gains to Belarus as well. The paper by the *Center for International Economic Studies, Academy of Sciences of Belarus – CIES (Belarus)* estimates that exports increased by around USD 200 million; the net effect for GDP amounted to about USD 80 million (about 3.4% GDP). As for non-tariff and anti-dumping measures, Belarus’ loss due to the NMS’ adoption of EU trade policies is estimated at around USD 50 million annually.

The papers dealing with Ukraine address the labor market adjustment costs of trade liberalization (*O. Pindyuk, Ukraine*), issues related to state aid and the challenges of relocating economic activities from the NMS to Ukraine (*International Centre for Policy Studies – ICPS, Ukraine*). Estimates show that the changes in tariffs have not significantly affected Ukraine’s labor market, while the decrease in non-tariff barriers positively influenced wages and had a negative impact on employment. The decline in labour market rigidities had a positive impact on employment and a negative one on wages. The amount of state aid in Ukraine has recently been reduced, yet so far without any institutional changes. The adopted decisions are unsustainable; the future policy-making remains unpredictable. The resulting inefficiency and inconsistency of state aid allocation is costly. The paper concludes that given the risks of price volatility and the need to implement a number of international commitments, Ukraine’s government should introduce new institutions and procedures for a more efficient allocation of state aid. Ukraine still lags behind the NMS in attracting foreign investors – despite its lower labour costs, relative freedom from costly EU regulations, and a more dynamic domestic market. The ICPS expects more greenfield investments in Ukraine at the expense of the NMS over the next ten years, yet no relocation of existing businesses. The analysis shows that Ukraine will maintain wage competitiveness over the entire forecast period. However, improvements in the business environment and progress in liberalizing trade relations with the EU will have a very significant impact on Ukraine's potential for business relocation.

Russian outward investments in the CIS represent a relatively recent and not sufficiently investigated phenomenon. Two papers by the *Turku School of Economics and Business Administration – TSEBA (Finland)* illustrate how Russian investments (often via third countries and not captured by the official statistics) dominate the energy and telecommunications sectors in most CIS countries and in this way exert a considerable leverage in the region. Even in Finland, which almost fully depends on Russia regarding energy imports while Russia is the largest export market for Finnish manufactures, the dependency on Russia requires mutual strategic partnerships and investment cooperation.

Last but not least, the latest set of INDEUNIS papers includes also studies on Moldova and Kazakhstan which investigate country-specific restructuring experiences and trade integration. A case study on Russia's automotive industry (by DC RF), as well as a more academic paper dealing with intra-industry trade and related labour market adjustment costs in selected EU countries (by the *Institute of Economics, Hungarian Academy of Sciences – IE HAS, Hungary*), were conducted as well.

On the whole, the INDEUNIS research results show that EU enlargement has had largely positive – if only small – effects on the Newly Independent States. WTO accession and closer EU-NIS integration are seen as desired targets though the Russian views regarding specific integration strategies sometimes differ from those of the remaining NIS, particularly Ukraine. There is a broader agreement in the project team that simultaneous EU-NIS integration would bring more benefits to all parties concerned.

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For additional information please consult either INDEUNIS website:

http://www.wiiw.ac.at/e/research_networks_indeunis.html

or the INDEUNIS project coordinator:

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