

THE ROLE OF THE TRADE REGIME

Trade Policies and Institutions

Introduction

The demise of central planning in Eastern Europe and the former Soviet Union over the period 1989–1992 resulted in the disintegration of the domestic mechanisms of control, such as the Council for Mutual Economic Assistance, that these countries had used to manage international trade with the rest of the world and with each other. At the same time, the political disintegration of the Soviet Union leading to the establishment of 15 new independent states and the breakup of Yugoslavia into 7 states resulted in a breakdown of the traditional links between economic units located in the territories of the new states: what had been domestic transactions in the same currency governed by the same laws and procedures became international trade requiring goods to cross national frontiers into different customs territories, be subject to different regulations, and involve payments in different currencies.

The combined effect of the transition from central planning to market rules and the political disintegration of the Soviet Union and Yugoslavia forced major adjustments to the trade patterns, both among the countries in the Region and with the rest of the world. The pace of the adjustment and reintegration of these economies into the world markets varied considerably and depended on both

the countries' original situation and the breadth and speed of introduction of market-oriented reforms.

As trade policy is a key link in the transmission of price signals from the world market to domestic resource allocation, trade reforms were an important component of broader market reforms introduced by the early reforming countries in Central and Eastern Europe and the Baltics, as well as in some CIS countries like the Kyrgyz Republic and Georgia. In other countries, such as Uzbekistan and Turkmenistan, trade reforms have lagged because overall market reforms have been slow. Integration in the world trading system requires much more than trade policy, however. The establishment of macro-economic stability; effective, trade-related and, more generally, market-based institutions; the rule of law; and a supportive business climate are essential to effective participation in international trade and have markedly affected the reintegration of these economies into world markets.

A country's integration into world markets depends also on the trade policies of its trading partners and the access it obtains to their markets. There are three important market-access relationships for the transition countries in Central and Eastern Europe and the CIS that affect their overall integration in world trade: (a) the trade relationships among each other at the Regional and sub-Regional level; (b) their relationships with the European Union, the main external market for most of them; and (c) their relationships with the rest of the world, including China, the United States, and other developed and developing countries.

Integration at the Regional, European, and world levels requires countries to abide by the rules of conduct that govern the multilateral trading system. These rules have been established and are being implemented in the context of agreements administered by the World Trade Organization (WTO). Regional and sub-Regional arrangements and, to some extent and on a temporary basis, relationships with the EU, can be based on special rules and provisions. However, membership in the WTO and abiding by the rules that are globally set in that organization and that govern all trade relationships are essential elements, perhaps even necessary conditions, for full integration into the world trading system. In recognition of this, all but one of the transition countries (Turkmenistan) have either become members of the WTO or are involved in the often-lengthy process of acceding to the organization.

In the 15 years since the fall of the Berlin Wall, the degree of integration into the world markets achieved by the transition countries in Europe and the CIS varies enormously. There are three broad groups:

the first group of eight countries of Central and Eastern Europe (CEE-8) have become members of the EU and have thus completed integration into the world economy. The second group of the 12 CIS countries has achieved much less integration, and many of these countries are still not members of the WTO. And there is a third group of countries in Southeastern Europe that is participating in a stabilization and association process that will ultimately lead them to EU membership, and whose integration into the world economy is in between the other two groups.

In addition, there are other groupings of countries that cut across these three classifications: for example, there are countries such as Armenia, Azerbaijan, Bosnia and Herzegovina, Georgia, Moldova, Serbia and Montenegro, and Tajikistan that have experienced significant internal or external political conflict that has impeded reforms. There are also differences in the degree of integration within each group: Armenia, Georgia, and the Kyrgyz Republic have very liberal trade regimes, while Belarus and Turkmenistan have essentially maintained the patterns of trade control that characterized central planning. Many countries are participating in a variety of multiple but often ineffective bilateral or regional trade relationships. Turkey, part of the World Bank's Europe and Central Asia (ECA) Region and thus included in parts of this study, is different: it is not a transition economy, in the sense of having had to move away from a system of central planning, though it continues to grapple with problems in a large and inefficient state enterprise sector. It is also well integrated into the world trade system, as it is in a customs union with the EU.

The purpose of this chapter is twofold: to assess how trade policies and institutions, as well as market access issues, have affected the trade performance of transition economies in Eastern Europe and the Former Soviet Union over the last decade and a half; and to look into the future in order to analyze the challenges these economies face in achieving fuller integration in the international trading system, at the Regional, European, and global levels. The analysis will deal primarily with trade in goods. But the chapter foreshadows analyses of a variety of other factors affecting trade performance, such as policies on trade in services, foreign direct investment, and other behind-the-border policies, which are discussed in detail elsewhere in the volume.

The chapter focuses on the countries of Southeastern Europe (SEE) and the CIS of the Region.¹ This is a group of 19 countries, plus Kosovo, that, although part of Serbia and Montenegro, has a separate customs territory. The eight countries of Central and Eastern Europe that have recently become members of the EU have had to adopt the EU *acquis*, including all aspects of EU trade policy, rules, and institu-

tions; their policies and future challenges, following accession, are not discussed in detail in this chapter. The main questions regarding these countries that are addressed here relate to the implications of their EU accession for the remaining transition countries in the region. Turkey, a special case, will be dealt with separately.

Trade Policy

The formal trade policy regimes of the 20 transition economies in SEE and the CIS, especially the 17 that have become WTO members (see table 3.1), compare, on the whole, quite favorably with the trade regimes of developing countries at similar levels of income.² Tariff protection of domestic industry and agriculture in the transition economies is on average lower; the extent of protection through non-tariff barriers appears to be no greater; there is less recourse to contingent protection; and, unlike many developing countries in Africa and Asia, transition economies that are WTO members have bound 100 percent of their tariff schedules (see table 3.2). WTO accession by a number of these countries in the near future can be expected to result in further liberalization and increased stability of their trade regimes.

TABLE 3.1
WTO Members in the Region (as of December 2005)

Country	Date of accession
Czech Rep.	1 January 1995
Hungary	1 January 1995
Poland	1 January 1995
Romania	1 January 1995
Slovak Rep.	1 July 1995
Slovenia	30 July 1995
Bulgaria	1 December 1996
Kyrgyz Rep.	20 December 1998
Latvia	10 February 1999
Estonia	13 November 1999
Georgia	14 June 2000
Albania	8 September 2000
Croatia	30 November 2000
Lithuania	31 May 2001
Moldova	26 July 2001
Armenia	5 February 2003
Macedonia, FYR	4 April 2003

Source: WTO.

TABLE 3.2
Average Applied Tariffs and Bound Rate by Country or Group in the Region in the Most Recent Available Year

Country/group	Average applied tariff rate (%)						Average bound rate (%)		
	All goods		Agricultural goods		Industrial goods		All goods		
	Simple avg.	Wght. avg.	Simple avg.	Wght. avg.	Simple avg.	Wght. avg.	Simple avg.	Wght. avg.	Binding coverage
EU-8	5.1	4.5	13.5	12.8	4.5	4.0	10.6	7.9	99.1
CIS-12	8.0	7.1	11.2	9.7	7.7	6.8	7.6	8.4	33.3
SEE-8	9.8	7.5	26.4	18.1	8.4	6.3	19.3	24.6	71.4
The Region	7.8	5.8	16.4	13.0	7.1	5.2	12.4	10.4	59.0
The Region and Turkey	7.5	5.1	16.7	13.0	6.7	4.5	14.2	12.0	59.6
Developing countries	11.9	9.2	16.6	16.7	11.5	8.5	38.1	19.4	58.9
EU-15	4.4	3.1	6.2	5.2	4.2	3.0	3.9	3.0	100.0
Memo:									
Turkey	3.0	2.0	21.8	12.7	2.0	1.3	28.6	19.8	49.9
Russian Fed.	10.8	8.9	9.8	8.9	10.9	8.9	n.a.	n.a.	n.a.

Sources: UNCTAD TRAINS and WTO IDB databases.

Note: n.a. = not available.

There are of course substantial differences among the trade regimes of the transition economies. At the one extreme are three very protectionist regimes in Belarus, Turkmenistan, and Uzbekistan.³ At the other extreme are recent WTO members like Albania, Armenia, Croatia, Georgia, the Kyrgyz Republic, and Moldova with very liberal trade regimes, especially when compared with developing countries at similar levels of per capita income. In between are some of the larger transition economies such as Russia and Ukraine.

Throughout the Region, trade is also impeded by lingering political conflicts resulting from the breakup of the Soviet Union and Yugoslavia. The unresolved conflict over Nagorno-Karabakh has resulted in a breakdown of economic relationships between Armenia and Azerbaijan, and Turkey has closed its border to Armenia. There are two quasi-independent entities, Abkhazia and Transdniester, whose administrations survive through support from Russia, but which have received no international recognition and continue to exist in a state of political confrontation with Georgia and Moldova, respectively. Both entities have become “black holes” in terms of formal trade transactions and the location of enterprises or individuals engaging in criminal economic activity; illegal arms transactions; and smuggling of cigarettes, liquor, and oil products (World Bank 2004f). This illegal trade results in significant revenue losses for the Georgian and Moldovan authorities. In the Balkans, there are still no significant economic relationships between Serbia and Montenegro and Kosovo, Serbian territory temporarily being administered by the United Nations.

Policies on Imports

Tariffs

Average Most Favored Nation (MFN) tariffs for countries in transition range from a low simple average of 3.3 percent in Armenia to a high of 11.5–11.6 percent in Belarus and Romania (see annex table 3.1). Averages weighted by imports are lower in all countries. Following a worldwide pattern, tariffs in general are much higher in agricultural than in nonagricultural sectors.⁴

Countries that have joined the EU (the EU-8) had on average lower tariffs than did other transition economies (table 3.2). Indeed, Estonia and Latvia had some of the most liberal trade regimes in the world. In contrast, tariffs in the CIS and the SEE are on average slightly higher. Still, their applied tariffs are on average somewhat lower than those of developing countries as a whole. On the other hand, tariffs on agriculture in the Southeastern European countries are on average higher than those in developing countries as a group. Turkey has increased its international integration as a result of its close interaction with the EU; see box 3.1.

BOX 3.1

Turkey's Trade Policies and Institutions

Turkey's integration into the world economy is strongly influenced by its increasingly close links to the European Union. In 2004, Turkey, already a WTO member, formally became a candidate for EU accession. Turkey has already established a customs union with the EU, and its trade policies and institutions are shifting in order to harmonize better with those of the EU. Turkey has initiated a number of macroeconomic stabilization programs in recent periods. While macro stability has been restored, the situation continues to be fragile, as inflation rates and the public debt continue to be at high levels.

Turkey's MFN tariffs are relatively high, averaging 11.8 percent in 2003. Because of the customs union with the EU, however, Turkey applies the much lower EU external tariff on industrial imports. Turkey also has a free trade agreement (FTA) on industrial products with the European Free Trade Association (EFTA) and has signed 14 other bilateral FTAs, as it tries to harmonize its trade regime with that of the EU. In agriculture, protection is quite high, with ad valorem rates ranging up to 227.5 percent for animal products. State support for agriculture is also substantial, and, as a consequence, the agricultural sector has become insulated from the world market. The government is in the process of implementing a wide-ranging five-year program (2001–2005) to restructure the sector by phasing out some of the more distorting measures such as administered prices, as well as production and export subsidies.

Broadly speaking, tariffs in most countries do not provide for a large degree of protection, although there is, of course, significant variation by country and sector. Armenia, Croatia, Georgia, and the Kyrgyz Republic, for example, have low average tariff rates with relatively little dispersion. Russia's average applied tariff rates average 10.8 percent, with highs of 50 percent in beverages. Import-weighted applied tariff rates average 8.9 percent. The tariff schedules for Belarus, Kazakhstan, and Russia are very close to the Russian tariff schedule because of the proposed customs union among these countries. The highest tariff protection in agriculture appears to be present in Bulgaria and Romania, while the highest tariff protection in manufacturing is in Belarus, Romania, and Uzbekistan (annex table 3.1). However, the tariff data are in some cases incomplete, as they do not include specific tariffs present in many countries' agricultural schedule.⁵ Also, it is unclear whether the "applied" tariffs in table 3.2 and in the annex take into account the preferential rates applied by many countries as part of their participation in preferential trade arrangements.

The main nontariff barriers (NTBs) are in textiles, where Turkey maintained a quota regime based on the international Agreement on Textiles and Clothing (ATC), which, however, expired in 2005. Since 1995, Turkey has initiated 46 antidumping (AD) investigations and taken definitive measures in 33 cases. AD actions have focused on textiles (China), plastics (EU), and steel (Russia, Ukraine). Turkey itself has also been the target of a slightly smaller number of antidumping actions over the same period.

The government operates a number of schemes to promote exports in the form of finance, insurance, guarantee, promotion, and marketing assistance. Several export credit programs are operated by the Central Bank, as well as several schemes providing incentives to small and medium enterprises (SMEs).

Services is the largest sector in terms of contribution to the GDP (about 65 percent); it faces a number of structural problems, including the existence of a number of inefficient, loss-making public sector enterprises. The government has taken some measures to extend privatization and liberalization in several sectors, notably banking and telecommunications. However, public companies continue to dominate most service provision and either operate as monopolies or hold exclusive rights. And foreign direct investment inflows are much lower than they could be.

Turkey faces major challenges in the near term as it attempts to deal with deep-seated structural problems in its state enterprise sector, harmonize its policies with the EU, and maintain macroeconomic stability. Further privatization and reforms of the services and agricultural sectors can make important contributions to its future growth and competitiveness; they will also help pave the way for EU accession.

Source: WTO Trade Policy Review 2003.

Many of the countries have a relatively small number of tariff bands, and low dispersion of tariff rates. Indeed, in the early 1990s, under the influence of advice from international financial institutions (IFIs), a few of the countries (Georgia, the Kyrgyz Republic, and, most recently, Kosovo) had established uniform tariff regimes that were subsequently differentiated as a result of pressure from domestic interests to raise tariffs on final goods; this was also a response to external demands for tariff reductions (“zero for zero” and other specific requests) on raw materials and intermediates at the time of WTO negotiations. The Kyrgyz Republic had a flat 10 percent tariff that applied to all products, but while maintaining a liberal trade regime, it ended up with several bands following WTO accession. Until recently, Kosovo also had a flat 10 percent tariff; however, under pressure from domestic interests seeking to obtain higher rates of effective protection for final goods, this is in the process of changing to provide for lower tariffs in selected raw materials and intermediate inputs. Ukraine had 50 tariff bands in 2003 compared with seven a decade before.

For the nine economies of SEE and the CIS that are WTO members,⁶ tariff schedules have been bound 100 percent; in most cases (the exceptions are Bulgaria and Romania), bound levels have been established that are close to those applied.⁷ Binding tariffs at close to applied levels provides stability to the trade regime, which is an important attraction for foreign direct investment, as well as a good defense against future domestic pressures to increase protection. In the case of Georgia, for example, domestic pressures resulted in increases in applied tariffs to closer to the bound levels after WTO accession (World Bank 2003c).

Taxation of imports is a significant source of revenue for most countries (for example, 71 percent of revenue in Armenia). The bulk of this taxation involves value added taxes (VAT) and excise taxes that are collected on imports. Tariffs are but a small percentage of the total, usually amounting to less than a quarter of trade taxes. Most tariff regimes yield far fewer revenues than the average MFN tariff level would suggest, however. For example, in Ukraine, the yield is about half the weighted average applied tariff rate. In Georgia, the yield is about a quarter. There are several reasons for this: first, there are many preferential arrangements that result in large segments of international trade entering duty-free; second, there are frequent ad hoc exemptions and exceptions; third, highly differentiated tariff structures, combined with weak and corrupt customs authorities, yield little revenue, and in some territories (for example, Albania, Bosnia and Herzegovina, Kosovo, and Tajikistan, there is widespread

smuggling. A simpler and less differentiated tariff structure would be easier to enforce and would yield more revenues.

In most countries, there is tariff escalation, usually resulting in significantly higher effective rates of protection for final products than for intermediates and raw materials. Examples of such high rates abound in the wood, leather, and textiles sector (World Bank 2004q). These high effective rates of protection for domestic industry result in inefficient resource allocation as well as in reduced incentives to export.

Nontariff Barriers

The Region's economies that have become members of the WTO have eliminated formal nontariff barriers (NTBs) on imports, except as allowed by the WTO. This means that some of them (Bulgaria, Romania) have imposed tariff quotas in agriculture, and all are using licensing procedures for imports aimed at maintaining sanitary, phyto-sanitary, and safety standards, as well as protecting the environment.

NTBs on imports are more common in non-WTO members in the Region. For example, Uzbekistan has nonautomatic licensing procedures for foreign exchange allocation through the banking system aimed at controlling both the overall level and the composition of imports, depending on the degree of "essentiality" of the imports. Ukraine uses its technical standards system as a vehicle for controlling imports into various sectors (World Bank 2004q). Serbia and Montenegro have a combination of licensing and quotas on steel imports (EC 2004). And several CIS members have used temporary import bans against selected neighbors as weapons in a variety of bilateral trade disputes or as emergency measures. For example, Russia and Ukraine have engaged in a number of bilateral disputes involving mutual bans of trade in certain commodities (see box 3.2); Uzbekistan has cut off imports from the Kyrgyz Republic in retaliation for nondelivery of electricity; and Kazakhstan has imposed prohibitive duties on trade with neighboring countries to deal with balance of payments problems. Using trade as a weapon in settling disputes is counterproductive and tends to hurt both countries in the dispute.

The IMF calculates an index of NTB restrictiveness ranging from open to moderate to restrictive; such categories are based mainly on the number of sectors covered by NTBs, the number of stages of production covered by NTBs, and the severity of the NTBs (see table 3.3). NTBs are defined to include quantitative restrictions, state trading monopolies, restrictive foreign exchange practices, quality or standards controls, and customs procedures. Over the period 1997–2003,

BOX 3.2**Russo-Ukrainian Trade Wars**

In 1999, Ukraine imposed special quotas on imports of electric filaments, artificial furs, and worsted canvas from Russia. In 2000, some polyurethane products were added to the list. The same year, Ukraine replaced the quota on filaments with an antidumping tariff of 97.5 percent for a period of five years. Russia responded with imposing antidumping tariffs on Ukrainian metal pipes. In 2001, after bilateral negotiations, the Russian antidumping measures on pipes were lifted and replaced with negotiated quotas. In 2002, Ukraine imposed an antidumping tariff on crossing pieces and threatened to impose tariff quotas on a variety of Russian products from the light and chemical industries, if Russia reintroduced a special tariff on Ukrainian metal pipes, which it was considering. That year, Russia introduced higher tariffs on Ukrainian zinc, steel, some metal products, and candies. In retaliation, Ukraine introduced a higher tariff on automobiles with an engine capacity of 1,000–1,500 cc, the engine capacity of most Russian automobile production and exports to Ukraine. In 2003, the informal agreement between the presidents of the two countries to lift all contingent protection measures affecting mutual trade was disavowed by the governments of both countries (World Bank 2004q).

Belarus, Turkmenistan, and Uzbekistan were assessed as having the most restrictive NTB policies; Armenia, Croatia, the Kyrgyz Republic, FYR Macedonia, Moldova, and Tajikistan received ratings indicating the least restrictive policies.

While formal nontariff barriers to trade continue to be a problem in several countries in the Region that are not members of the WTO, a far greater problem is posed by informal barriers that impede trade in all countries. Many of these barriers result from institutional weaknesses or weak infrastructure, for example in transport or finance, and are discussed below in part III of this study. However, many other impediments that result from government policies involving the issuance of licenses and other permits for the movement of goods across frontiers act as formidable, albeit informal, barriers to trade. A recent study of nontariff measures that impede trade in SEE found that there were few formal NTBs in the Region. However, trade was impeded significantly by a variety of government rules, procedures, and other requirements that caused delays and impeded trade (EC 2004). Similar problems have been identified in other countries, such as Armenia, Georgia, Moldova, and Ukraine, where this issue has been addressed (World Bank 2002a, World Bank 2003c, World Bank 2004f).

TABLE 3.3
IMF NTB Trade Restrictiveness Ratings: 1997–2003

Country name	NTB rating		
	1997	2000	2003
Albania	2	1	1
Armenia	1	1	1
Azerbaijan	2	1	1
Belarus	3	3	3
Bosnia & Herzegovina	2	1	1
Bulgaria	2	1	1
Croatia	1	1	1
Czech Rep.	1	1	1
Estonia	1	1	1
Macedonia, FYR	1	1	1
Georgia	2	1	1
Hungary	2	2	2
Kazakhstan	2	2	2
Kyrgyz Rep.	1	1	1
Latvia	1	1	1
Lithuania	1	1	1
Moldova	1	1	1
Poland	1	1	1
Romania	2	1	1
Russian Fed.	1	2	2
Serbia & Montenegro	...	3	2
Slovak Rep.	1	1	1
Slovenia	1	1	1
Tajikistan	1	1	1
Turkmenistan	3	3	3
Ukraine	2	2	2
Uzbekistan	3	3	3
Turkey	2	2	2

Source: International Monetary Fund.

Note: The data for the EU-8 are for barriers that existed before their EU accession.

Contingent protection involves protection that a country imposes in response to actions by its trading partner(s) that are supposed to have an adverse impact on its domestic production, employment, or trade. The main forms are safeguards against an influx of imports that threaten to cause serious injury to domestic industry, countervailing duties against export subsidies, and antidumping measures against practices of dumping. In the last decade, antidumping has been the favorite instrument of protection of industry worldwide (see table 3.4). Compared with other instruments of protection, antidumping actions are less transparent and can lead to reduced competition and cartelization of the affected sectors (Finger 1993). Transition countries have introduced the necessary legislation, but

TABLE 3.4

Number and Share of Antidumping Investigations by Initiating Country, 1995–2003

Initiated by	Initiated against				
	Industrial countries ^a	Developing countries ^b	Of which: China ^c	Transition countries ^d	All countries
Number of antidumping investigations					
Industrial countries ^a	226	574	129	132	932
Developing countries ^b	453	827	225	173	1,453
Transition countries ^d	4	7	2	20	31
All countries	683	1,408	356	325	2,416
Share of antidumping investigations					
Industrial countries ^a	0.24	0.62	0.14	0.14	1
Developing countries ^b	0.31	0.57	0.15	0.12	1
Transition countries ^d	0.13	0.23	0.06	0.65	1
All Countries	0.28	0.58	0.15	0.13	1

Source: WTO Antidumping Committee.

Note:

a. Includes Australia, Canada, 15 European Union members, Iceland, Japan, New Zealand, Norway, Switzerland, and the United States.

b. Includes all other countries and China, excluding industrial and transition countries.

c. Excludes Hong Kong (China), Macao, and Taiwan (China).

d. Refers to the 27 transition countries in the Region, and excludes Turkey, with 61 initiations.

until recently had relatively limited recourse to antidumping or other contingent protection remedies. Until 1997, only Poland had initiated a number of antidumping investigations (in 1991), but did not actually impose antidumping measures (Miranda et al. 1998). Since 1995, six countries (Bulgaria, the Czech Republic, Latvia, Lithuania, Poland, and Slovenia) initiated a total of 31 antidumping investigations (see annex table 3.2). All of these countries except Bulgaria have by now become EU members, and the measures have been terminated. More than two-thirds of their investigations were directed against neighboring transition economies, most commonly Belarus. Cement (Latvia and Lithuania), rubber products (Lithuania), and pocket lighters (Poland) were among the items most frequently protected. The above data do not include antidumping measures taken by some CIS countries (for example, Ukraine and Russia), which are not members of the WTO, against each other, as well as against the EU and the United States; these measures are typically in retaliation for antidumping or other measures taken against their own exports (World Bank 2004q). To the extent that these actions are still in place at the time of these countries' accession to the WTO, they would have to be reviewed for their conformity to WTO provisions.

Policies on Exports

Export performance of the Region's economies has suffered simply because production of traditional export commodities has declined as part of the overall decline of production following the onset of transition. Compared with the 1980s, production of traditional exports of wine, fruits, and vegetables declined by more than 70 percent in Georgia and Moldova. Sheep exports virtually disappeared in the Kyrgyz Republic. In other cases, whole sectors turned out to be uncompetitive in market conditions: Bulgaria's computer industry, which was thriving in the sheltered environment of the CMEA, disintegrated in the face of international competition.

Other than the EU-8, most countries in the Region found it difficult to develop new exports. This was due to many factors, but in part it was a result of their own policies. Governments of transition economies, especially non-WTO members, on the whole have exhibited a tendency of taxing rather than subsidizing or supporting exports. Policies discouraging exports are in part a legacy of their planned economy days, when "keeping the goods at home" was given the highest priority and exporting was focused on disposing of surplus production. These taxes and controls have had an adverse impact on export performance for countries that have employed them.

Most transition economies tax exports of fuels and raw materials. They do this for two reasons: first, for revenue purposes, to compensate for the absence of an effective system of taxing the exploitation of natural resources; and second, in order to promote domestic industry by permitting it to obtain raw material inputs at lower than world prices. Export taxes on raw materials—and in some cases on food—exist in Belarus, Bosnia and Herzegovina, Russia, Serbia and Montenegro, and Ukraine. There are also licensing requirements or other controls on the export of natural-resource-based products such as timber (in Georgia and Moldova). A number of countries (for example, Azerbaijan, Georgia) ban the export of scrap metal. In the case of Georgia, these controls do not appear to affect the overall level of exports, but simply to drive some of the exports underground.

The most restrictive export controls are operated by Uzbekistan. In that country, there is a system of forced government procurement of cotton, which effectively taxes producers by giving them substantially less than world prices, and state monopolies on exports of cotton, minerals, and precious metals. State trading activities in Azerbaijan (oil), Tajikistan (aluminum), and Turkmenistan (oil and gas) are used as the main instrument of control and regulation of exports.

Export taxes and other controls on raw material exports also introduce inefficiencies in the allocation of resources and need to be progressively phased out. When the main objective is capturing rents from natural resource exploitation, taxes on resource depletion are more efficient and need to be introduced. When the objective is to stimulate industry, assistance can be provided in ways that do not discriminate between the domestic and external markets.

Exporters are also disadvantaged by the lack of effective and timely rebates on tariffs, VAT, and other taxes affecting imported inputs. While most countries in the Region have put such systems in place, they have not operated efficiently. For example, rebates are provided with significant time lags, with the result that exporters are penalized and put at a competitive disadvantage with foreign suppliers, who can obtain their inputs at world prices (World Bank 2003c, World Bank 2004d, World Bank 2004f, World Bank 2004q).

While on the whole, the Region's policies have tended to disadvantage exporters, some countries that are not WTO members have provided subsidies to important export industries. This has been the case for steel in Ukraine and a number of products in Serbia and Montenegro. Similarly, Tajikistan's aluminum exports would not be viable without significant subsidies to electricity. Subsidizing exports is a drain on the budget and cannot be afforded by many of these countries, which have been facing serious budgetary constraints. In any case, many of these subsidies are not WTO-consistent and will have to be eliminated when these countries accede to that organization.

Finally, a number of countries in the Region have introduced Export Processing Zones and similar arrangements to provide tax-and-duty-free arrangements for exports. Such arrangements have been shown to have the potential for providing a stimulus to exports in several developing countries. Unfortunately, there is little evidence that these arrangements have been effective in stimulating exports from transition economies in the Region that have them (see chapter 4).

There are, nevertheless, a few bright spots in the export performance of economies in the Region that are worth discussing in some detail because of the implications they have for other economies in the Region. Romania is one example of a very impressive export performance, both in terms of reorienting its trade to the European market and in sustaining its expansion in the presence of significant competition from low-cost international suppliers in such sectors as textile and shoes. The key to its success appears to be its ability to participate effectively in international networks of production and distribution. Falling transportation and communication costs create

opportunities for outsourcing. Value chains are becoming increasingly split, with individual production stages moving to countries to exploit their comparative advantage. In the case of Romania, the driving force has been Italian firms that have organized the insertion of Romanian firms into global networks of production and distribution of footwear and clothing (World Bank 2004i). Their efforts have been able to overcome a strongly protective tariff regime that acts as a general disincentive to exports. Many other successes in the region are discussed in detail in chapter 7.

Future Challenges

Although, overall, the existing trade regime is not a major problem of trade policy for most of the Region's countries, there is still room for improvement and a variety of challenges. On imports:

- Countries acceding to the WTO can use the accession process to further liberalize their tariff schedules and bind them at levels that are close to applied. To the extent possible, such countries need to resist domestic pressures to raise protection on final goods (or seek to establish bindings for tariffs at substantially higher levels than previously applied), as well as external pressures to reduce tariffs on a variety of raw materials and intermediates, which would result in raising effective rates of protection in various product chains.
- Countries that are already WTO members need to use the ongoing WTO multilateral trade negotiations as an opportunity to further reduce their applied and bound tariffs in exchange for improved market access for their own products. While autonomous tariff liberalization can be beneficial to any country that undertakes it, multilateral trade liberalization through international agreements has the potential of yielding even greater benefits and may be easier to accomplish domestically in light of the political-economy power of vested interests "behind the border."
- Nontariff barriers are of importance in a number of countries that are not WTO members. These barriers should be substituted by tariffs as early as possible; they will have to be dismantled as part of the WTO accession process, in any case.
- The challenge for the many countries in the Region that have so far avoided using antidumping measures is to continue this policy because, while antidumping is a popular instrument of protection worldwide, it entails large costs to the domestic economy.

- All of the Region's countries would benefit from measures that increase revenue yields from existing tariff regimes through strengthening the customs service and reducing corruption and smuggling, as well as eliminating formal exemptions to tariffs.

The main challenges transition economies face in promoting their integration into the world economy through an expanding export sector are to

- establish efficient taxation of raw material exploitation at the source and phase out export taxes;
- provide support, where appropriate, for industrial development through WTO-consistent measures that do not discriminate between domestic and export markets;
- establish efficient tariff, VAT, and other import tax-rebate systems; and
- attract export-oriented FDI to help them integrate into worldwide production and distribution chains.

Institutional and Other Domestic Constraints

The preceding analysis of trade policies in the Region suggests that, aside from a general bias against exports, in most countries the formal trade regime has not hindered their integration into the world economy. Yet, in some countries with very liberal regimes toward imports, the question, "We have done everything to liberalize our trade. Why is our trade performance worse than it was under central planning?" is frequently heard. The response to this question is multifaceted and has to do in part with the bias against exports mentioned above. Mainly, however, it is because serious weaknesses in market- and trade-related institutions and infrastructure continue to undermine effective participation of these countries in international trade. They also undermine the opportunities that trade policy reform can increase growth and reduce poverty; see box 3.3. Subsequent chapters will analyze these institutional and domestic constraints in detail. Here we develop the context for that discussion and highlight some of the more salient issues.

A fundamental problem is an interventionist attitude on the part of governments. Such an attitude is pervasive in practically all aspects of market activities, but it has a very stultifying effect on international trade and has been identified as a key constraint in export development in virtually all of the countries in the Region. In the Kyrgyz

BOX 3.3**The Interrelationships between Trade, Growth, and Poverty Reduction in the Region**

Trade performance is one of many factors that affect GDP growth and, through growth, the reduction of poverty. Trade performance in turn is affected, in part, by trade policy. The effect of trade policy on poverty via its effect on growth is, necessarily, more complex. The transmission is indirect and manifests generally only over a relatively long term. At the same time, however, trade policy results in changes in relative prices, which will have a short-term impact on the welfare of the poor, by affecting both their employment and income prospects as well the prices of the goods they consume. Based on the outcomes of trade-policy reform in developing countries, a great deal of analysis exploring the impact of liberal trade regimes on economic growth has been carried out in recent years. The preponderance of empirical evidence from developing countries worldwide suggests that, on average, growth will be enhanced in the long run as a consequence of liberal trade regimes.^a

As is the case elsewhere in the world, disentangling the linkages between trade and poverty reduction in the Region is more complex. As is well known, there was, for several reasons, a massive increase in poverty in the Region at the onset of the transition.^b Despite the fact that most of the Region's countries early on adopted (and have largely maintained) relatively liberal formal trade regimes and that, moreover, substantial progress in poverty reduction has been made in the Region in recent years, today—more than a decade after the onset of transition—widespread poverty persists in several of the Region's countries, especially, but not exclusively, in Central Asia and the Caucasus.

There have been some efforts to analyze through simulations the implications of specific trade-policy reforms on poverty in individual countries in the Region. However, there is no aggregate assessment of the experience for the group as a whole. The individual countries for which assessments have been made are Bulgaria, Moldova, Romania, and Russia.^c These analyses generally find that the effect of trade liberalization on the poor as a group would tend to be positive.^d However, there is also evidence that trade liberalization would likely reduce the well-being of some people, at least in the short term, and that some of these would be the poor, who can ill afford it.^e

On the other hand, the absence of trade liberalization does not always translate into the poor becoming better off. The case of the slowest-reforming countries—such as Belarus and Uzbekistan—is instructive in this regard. Although their decreases in output and increases in poverty have been more limited than those of other countries in the Region, in part because of the maintenance of relatively closed trade regimes, they have nonetheless engaged in policies, such as the protection and state control of the cotton sector in Uzbekistan, which have been adverse to the welfare of the poorest elements of society.

(Box continues on the following page.)

BOX 3.3 (continued)

If the assessment of the implications of trade reform on poverty in the Region's transition economies is sobering—in the sense that in the short run, poverty will likely increase in certain segments of society—it is not inconsistent with the analysis in other countries worldwide. Retrospectively, greater exposure to trade may well have exacerbated poverty in the CIS countries. The situation was much better in the EU-8 and SEE economies, however, probably because many of these countries quickly pursued policies that provided for greater flexibility in resource allocation. These policies permitted workers displaced by imports, as well as new labor force entrants, to be employed in new labor-intensive activities; they also focused on facilitating exports. Thus, in the absence of effective product and factor markets, the adjustment to trade reforms in the CIS has been very protracted. In consequence, the “short run” for these countries may still be lingering.

Despite the variations in these findings, there is a general consensus that, for the poor to gain from trade liberalization, actions that complement trade reform are needed. The main conclusions of individual country case studies—as well as cross-country econometric studies—that have looked at experiences with trade liberalization at the country level worldwide are the importance of enhancing flexibility in labor markets and facilitating the flow of investment from sectors that are contracting to those that are expanding. In short, a policy of import liberalization alone is not sufficient to promote the strong trade performance that could be beneficial to output growth and indirectly to poverty reduction. A variety of additional reforms needs to be implemented for such a policy to have meaningful and enduring salutary effects.

a. Over the 1990s, the proposition that trade openness is good for economic growth was advanced by a number of cross-country studies (Sachs and Warner 1995; Edwards 1998; Dollar and Kraay 2001). But the findings of some of these studies have been subjected to serious criticism: restrictiveness of trade policy is difficult to measure, and the openness indicators used to show links to growth are not good proxies for trade policy. Institutional development, in a broad sense, has been proposed as a factor that explains both trade and output growth (Rodriguez and Rodrik 2001). Experience has shown that, in the long term, countries need an open economy to sustain growth. However, developing country experience has shown that, for a time, countries have expanded their exports and trade under different kinds of trade regimes. Some, like China, Korea, and Taiwan (China), have done so under complex trade regimes that provided extensive import protection while at the same time providing very substantial stimulus to export industries. Successful implementation of such complex policies involving both import protection and stimulus to exports places great demands on foreign trade policy design and trade institutions, which few developing or transition countries can meet (World Bank 2002d). Others, like Chile, Hong Kong (China), and Singapore, have expanded exports while maintaining a very liberal regime on imports. Still others, like Mauritius and El Salvador, have used export processing zones to stimulate growth in trade, while maintaining substantial import controls.

b. World Bank 2000b and 2005b.

c. See Rutherford, Tarr, and Shepotylo (2004); Porto (2004a); Csaki et al. (2000); Csaki et al. (2002).

d. See, for example, Winters et al. 2004.

e. See, for example, IIED (2004); World Bank (2003c); Nicita (2004); Chen and Ravallion (2004).

Republic, the majority of businesses are required to obtain more than 30 permits in a six-month period after start-up to legally conduct their operations (World Bank 2004d). In Moldova, trade can play an important role in alleviating poverty, but this can happen only when

the range of informal barriers to both imports and exports—such as cumbersome and restrictive customs procedures, corruption, and burdensome and inappropriate regulation—are significantly reduced (World Bank 2004f). The business climate is seen as the major factor constraining Ukraine's integration into world trade (World Bank 2004q). Similar conclusions apply to virtually all transition economies where the role of trade in development has been analyzed.

At the same time, there are serious institutional weaknesses both of a general nature (for example, concerning enforcement of contracts and property rights), as well as in particular areas critical to international trade, such as the availability of trade finance and insurance, or the transparency of customs procedures. Because of weaknesses in government and judicial system enforcement, there are problems, even when the laws and regulations are in conformity with international standards. These weaknesses in the market mechanism tend to discriminate more against foreign suppliers and imports—just as they do against foreign investors. In addition, most countries in the Region face serious problems in their transport systems, which in some cases are combined with issues of remoteness as well as transit problems created by their neighbors; all of these raise the costs of imports and exports and undermine the countries' capacity to integrate into world markets.

Trade-Related Policies and Institutions

Macroeconomic and Exchange-Rate Policies

Macroeconomic instability and ineffective exchange-rate policies can pose serious constraints to international trade performance. In the period immediately following the breakup of the Soviet Union, macroeconomic instability and payments issues were a serious problem for international trade in the CIS countries and in the Baltics (Michalopoulos and Tarr 1996). Following the 1998 financial crisis in Russia, however, most countries restored macroeconomic stability. While there have been some problems, macroeconomic instability has not been a major issue affecting trade performance in most countries in the Region in recent years. Moreover, all countries, except Turkmenistan and Uzbekistan, have relatively liberal exchange-rate regimes, and several (Armenia, Georgia, the Kyrgyz Republic, and Moldova) have met IMF Article VIII standards.⁸

In the aftermath of the 1998 crisis, Russia found itself with a substantially devalued exchange rate, which resulted in giving strong incentives to production for export and import substitution. At the same time, countries dependent on the Russian market encountered

some difficulties. Several countries (Moldova, Kazakhstan, and the Kyrgyz Republic) had to devalue as well, after a period of real exchange-rate appreciation. In others (Armenia, Georgia), the overall real exchange rate appears to have remained relatively constant over the five-year period (1995–2000); in Armenia, however, the exchange rate continued to appreciate in relation to the ruble after 1998, contributing to the decline in competitiveness of Armenian products in the Russian market.

Real exchange-rate appreciation or fluctuating real rates or both have adversely affected competitiveness and the development of new export industries in some of the Region's countries at some points in time. For example, there is strong evidence that the Serbian exchange-rate policy of the last few years, while beneficial to maintaining domestic price stability, has adversely affected the competitiveness of the economy and that a different mix of macroeconomic policies is desirable (World Bank 2004k). In Azerbaijan, rapidly expanding oil exports were accompanied by a depreciation of the exchange rate after 1997, thus apparently avoiding the "Dutch disease" phenomenon, which adversely affects the development of new export products and the competitiveness of others (World Bank 2003a). On the other hand, other traditional export products—like cotton—have all but disappeared. Again, however, the exchange rate does not appear to have been a general problem for most countries in the Region.

Taxes

The tax system and tax administration are also important impediments to exports in many of the Region's countries. In Georgia and elsewhere, many firms complain that tax administration is arbitrary and unpredictable. The tax code is complex and changes frequently. Its administration is opaque, leading to opportunities to extract bribes (World Bank 2003b; World Bank 2003c; World Bank 2004d).

While, as discussed above, formal trade barriers are not very high, they often involve some cascading of tariffs. In addition, they always involve a VAT paid by all imports, usually in the neighborhood of 20 percent. As noted earlier, where exports depend on imported inputs, both tariffs and the VAT on inputs need to be promptly refunded or credited to the enterprises. This rarely happens, as evidence in country after country suggests (World Bank 2002d; World Bank 2003c; World Bank 2004d; World Bank 2004q). As a consequence, exporters are penalized and lose competitiveness. In the case of the Kyrgyz Republic, this factor alone (nonrefund of tariffs and VAT) is estimated to have raised total costs by 9 percent on 44 firms surveyed (Cuthbertson and Jones 2000).

Another problem present in the Kyrgyz Republic, and other countries in the Region as well, is the continued presence of high payroll taxes.⁹ These taxes lead to a variety of problems, including depression of official wages in order to avoid payment of the payroll taxes (World Bank 2004d). In the context of international trade, however, they have an especially distorting effect: arguably, an important comparative advantage of these countries lies in their supply of large numbers of educated and qualified labor. Taxing the use of this labor is a sure way of diminishing the competitiveness of their exports, current or potential.

Customs

The problems faced by the customs services of all economies in the Region are well known (see chapter 5).¹⁰ Customs services are only a relatively few years old and have not had adequate time to develop expertise. Customs officers are paid low salaries, both absolutely and relative to the private sector. Not only do they lack the resources of a modern customs service, including fully computerized systems and communications procedures such as mobile phones and e-mail networks, in Georgia, they even lacked uniforms for some time! Customs services are also expected to administer a complex and frequently changing set of rules and regulations including, but not limited to, the tariff. In Bosnia and Herzegovina, Georgia, Moldova, and elsewhere, they are not able to control large parts of the border. Even where there are customs posts (for example, in the Caucasus), the physical infrastructure is weak and probably would not be able to cope with significant increases in trade.

These difficulties are compounded in some cases by internal management problems. In the case of Georgia, there have been very frequent changes in the top customs administrator. In Azerbaijan, there are problems of coordination and communication among the different agencies involved in clearance of imported merchandise. In a number of countries in the Region (including Azerbaijan and the Kyrgyz Republic), approvals by the standards or health agencies take a long time and sometimes rules are capriciously enforced. Dispute settlement procedures are lengthy and nontransparent, leading participants to resort to bribes in an effort to resolve them. In the Kyrgyz Republic, approvals are needed from different agencies, which are physically situated in different parts of the country. In Armenia and Serbia and Montenegro, there is evidence that customs uses reference prices on imports, which is inconsistent with WTO provisions (World Bank 2002a).¹¹

The principal border crossings vary significantly in terms of staffing and facilities. In the Caucasus, even the best seem to have lit-

tle additional capacity to deal with any future increases in traffic volume and are likely to be the source of recurrent and substantial delays. In the case of Moldova, the problems do not seem to arise on the Moldovan side, but on the side of Ukraine. In the case of Central Asia, there appear to be few problems in the rail network crossings between Tajikistan and Uzbekistan, but there are serious issues in road transport that are discussed below, in connection with transit issues. Tajikistan has a long border with Afghanistan, which was patrolled by Russian troops; this, however, did not prevent significant smuggling.

The lack of coordination among the customs authorities in various territories that constitute the Region, such as the Caucasus, Central Asia, and Southeastern Europe, is a critical bottleneck to international integration. Some progress has been made in this regard in Southeastern Europe and, to a lesser extent, in Central Asia, through the establishment of mechanisms for periodic consultations among transport authorities, although many border crossing and transit problems persist. In the Caucasus, more collaboration is needed, even between the customs authorities not directly affected by the Armenia-Azerbaijan conflict.

In some countries (Georgia, Moldova, Uzbekistan), preshipment inspection (PSI) services have been put in place. These services have not been generally successful, however. In Georgia, the service was cancelled because it was not perceived to be cost-effective. In Moldova, there were complaints about the service that had been put in place in December 2001, and the decision was made to apply PSI only to final products. Firms complained about delays and costs, while customs officials complained of misclassifications. These problems may simply reflect the initial reactions of individuals who perceive the PSI as limiting either their authority or their freedom of action. And, clearly, PSI will fail if it does not have the support of the government and customs. Nevertheless, experience in many countries suggests that PSI is not a magic bullet that will solve all problems—it has to be supported by a thoroughgoing customs reform.

As discussed in greater detail in chapter 5, there are many elements to a customs reform, including internal organization of the customs authority; staffing; remuneration; performance management and accountability; automation and modernization of operational procedures consistent with international practices; introduction of internal/external control and audit procedures; physical infrastructure, both in terms of equipment for automated procedures and communication, and also for customs posts; simplification of approval procedures for various standards and health organizations; and more

effective coordination between customs and other organizations involved in controlling imports.

Services

In addition to customs, effective integration into the world trading system requires the support of a variety of other institutions and policies. The availability of low-cost, high-quality services is a critical determinant of export competitiveness. Research has shown that policies and projects that aim at decreasing the costs of services that facilitate trade produce economywide benefits that are a multiple of the benefits that result from trade liberalization (Hoekman 2002). The key services that facilitate trade are those involving banking and finance, marketing, and standards organizations, as well as telecommunications and transportation.

The economies of the Region emerged from the period of central planning with even more government controls and monopolies in the services sectors than those traditionally exercised by market economies. As discussed in detail in chapter 6, in the last decade, the introduction of market-oriented reforms in the services sectors has proceeded at a different pace in the various countries, as has the liberalization of merchandise trade. However, many service sector deficiencies remain in practically all of the transition economies, including the largest and strongest. In Russia, the realization is growing that almost all service sectors, including financial services, insurance, accounting, and business services, as well as legal services and construction, are in need of competitive restructuring. The same is true for transport, telecommunications, and utilities, which traditionally have been considered as reserved for government monopolies. In many of these sectors, technology change has made it possible to introduce competition; this leads to improved efficiency, a key to long-term competitiveness in international trade (Broadman 2004).

Countries in the Region that have joined the WTO have had to review their policies that affect international trade in services when they made commitments under the General Agreement of Trade in Services (GATS) in the context of their accession; others that are in the process of accession will have to do so in the future. Box 3.4 describes the GATS.

A useful taxonomy for describing international transactions in services is provided by the notion that they can be mediated through four supply modes. One case is where the user receives the service from the provider located in another country; this mode is referred to as “cross-border supply.” An example is the provision of architectural

BOX 3.4**The General Agreement on Trade in Services (GATS)**

The GATS accord was part of the Uruguay Round of negotiations, which began in 1986 under the auspices of the General Agreement on Tariffs and Trade (GATT) and concluded with the establishment of the WTO in 1995. The GATS represents the first attempt to devise a multilateral, legally enforceable understanding covering trade and investment in the services sector. Like the GATT, which was updated as part of the Uruguay Round and still forms the WTO's principal rule book for trade in goods, the GATS provides a legal basis on which to negotiate the multilateral elimination of barriers that discriminate against foreign services providers and otherwise deny them market access. The GATS differs from the GATT in several respects. Perhaps the most important difference is that the principles of national treatment (that is, nondiscrimination) and market access (that is, freedom of entry and exit) are provided automatically under the GATT, but are negotiated rights and obligations in the GATS. The negotiations on national treatment and market access for services in the GATS constitute the equivalent of tariff negotiations for goods in the GATT. In services trade, there is effectively no "border," as there is in goods trade. The restrictions on international transactions in services are embedded in countries' domestic laws, regulations, and other measures. Under the GATS obligations, these restrictions are liberalized (in varying degrees), thus creating for services a regime that is the equivalent of a duty-free regime for goods.

The GATS comprises two principal components. The first is a framework that sets out general multilateral rules governing trade and investment in services. The second complements the rules framework. It is the set of binding commitments to market access and national treatment for the individual services industries; countries append these commitments to the agreement in the form of a "schedule." Like tariff negotiations in goods, these multilateral services commitments result from iterative bilateral "request and offer" negotiations conducted seriatim on a country-by-country basis. Supplementing the rules framework are sectoral annexes and under-

blueprints via fax. A second mode is the case where a service can be provided through "consumption abroad," that is, with the consumption of the service taking place outside the user's home country and in the country of the supplier. An example of this is tourism. A third case is where the provision of the service requires sustained interaction between the user and the supplier of the service, and thus the service provider establishes a facility, or otherwise attains a "commercial presence" in the user's country. Typically, though not always, this mode means that foreign direct investment is part of the provision of the service. An example is the establishment of a foreign law practice in the host country. The final mode involves the need for close inter-

standings that contain specific rules dealing with, among other things, issues affecting financial services, aviation services, and access to telecommunications networks.

While some of the provisions of the overall rules framework apply to all services industries regardless of whether they are “scheduled,” many pertain only to industries for which market access or national treatment commitments are assumed. As a result, on balance, the GATS employs what has become known as a “positive list” approach: unless an industry is scheduled, it is, in the main, automatically excluded from the most meaningful terms of the agreement.

The fundamental mechanism of the GATS, which engenders the agreement’s multilateral liberalizing character, is the rule that also serves as the basis of the GATT: Most Favored Nation (MFN) treatment. Like the GATT, the MFN principle—that a signatory treat all countries in a manner no less favorable than its treatment of a particular country—generally applies to all services included in the GATS, regardless of whether a particular industry is included in a country’s schedule of commitments. However, the GATS allows for flexibility in the application of MFN. In particular, it permits exemptions to MFN for specific laws, regulations, and administrative practices. Such flexibility is essential because of the need to be able to maintain existing regulations or agreements not consistent with MFN, or the need to preserve the prospective use of reciprocal or unilateral measures, particularly when a country has concluded, as a tactical matter, that the GATS commitments offered by other countries for a specific industry generally are not sufficiently liberalizing.

In addition to the negotiated rights and obligations of market access and national treatment, as well as the MFN rule, other core provisions of the GATS include the requirement for countries to publish all domestic laws and regulations affecting services: these include assurances for due process in notifying interested services providers of the status of license applications; disciplines on public monopolies; rights governing the mutual recognition and harmonization of regulatory standards; consultation procedures on competition matters; and exceptions for national security, safety, and health, and the enforcement of tax laws.

Source: Broadman 1994.

action of user and provider, with the supplier located in the user’s country; however, it involves only the temporary presence of “natural persons” (usually referred to as “business persons”) for the delivery of the service. This situation can occur, among other ways, as an intracorporate transfer of a professional or on the basis of an individual entrepreneur operating under a contract. An example of the latter would be a foreign computer software consultant.

Of course, these various modes of supplying services are not mutually exclusive. All the modes of supply described above, taken together, can be usefully summarized as “cross-border trade and investment” in services. As the analysis above makes clear, barriers to foreign invest-

ment, as well as barriers to temporary movement of personnel, can be tantamount to barriers to services trade (see Broadman 1994).

In general, the SEE and CIS countries that have become WTO members have made more commitments to liberalize their services sectors in comparison to other countries at similar levels of economic development (Michalopoulos and Panousopoulos 2002). In terms of their overall commitments, these countries have made more commitments regarding national treatment than market access, a tendency common to virtually all WTO members worldwide. In addition, as in other countries, there were far fewer commitments for the provision of services through "mode four," presence of natural persons, than for the other three modes of supply. The sectors in which countries in transition made the fewest commitments are health, recreational, and transport services, while extensive commitments for liberal access were made for construction, distribution, tourism and travel, financial, business, and communication services (for further details, see chapter 6). In some cases (Bulgaria, Romania), the countries have liberalized sectors such as banking and finance *subsequent* to WTO accession, and their policies are in fact more liberal than their bound WTO commitments would indicate.

Banking and Finance

Despite these liberalization commitments, most of the financial institutions in many countries in SEE and the CIS do not appear capable of financing trade flows at present. Financial markets are poorly developed, and letters of credit, bills of exchange, and other modern payment instruments are unavailable. Payments between traders in the Central Asian countries can only be cleared through settlement accounts in commercial banks of neighboring countries. However, governments collect tax revenue on these accounts, and international clearing is tightly controlled.

Access to domestic credit by exporters is basically nonexistent. This is part of a general problem of unavailability of credit to small and medium enterprises, both because the banks see other, easier, and more profitable investment opportunities and because the creditworthiness of any company seeking credit is difficult to establish. As a consequence, credit has to be provided from the importing side, something that is obviously easier to do when selling to developed countries with well-developed financial sectors than when selling to Regional partners.

While trade finance is important, its provision should be part of an overall strengthening of the commercial banking system. International experience suggests that directed credit lines that are specifi-

cally designed for short-term trade finance do not have a lasting impact in the absence of a strong banking sector; further, there are a very few product lines in these countries that would require longer-term export credits. At the same time, given the weaknesses in the domestic banking sector, perhaps the best way of developing credit lines for trade is to promote the operation of foreign banks, which, with their international contacts, can help in trade finance.

Marketing Institutions

Marketing institutions are basically absent from much of the Region, and exporters have to rely on their own resources to market their products. For traditional raw material exports (for example, Uzbekistan cotton, Tajikistan aluminum), this is not a problem. Russia and, to some extent Ukraine, inherited much stronger marketing capabilities for traditional exports, which helped them preserve some high-value niches (for example, arms, nuclear, and space technologies). Russian suppliers also effectively substituted for other CIS enterprises that were parts of traditional Soviet chains (World Bank 2004p). The difficulties arise when a new product line has to be introduced. In such cases, marketing is easier when the export is based on a joint venture with an international partner who has established commercial links abroad. This has been a problem for many smaller CIS and SEE economies, as there have been few joint ventures in general and fewer yet outside the extractive industries.

Standards Organizations

Standards organizations operate in all of the countries in the Region. Traditionally, these organizations used Soviet-era standards, which increasingly have been modified to make them compatible with international standards. This is something that the countries in the Region that have become members of the WTO have had to do and that will have to be done by the others in the Region before they become members. Currently, the operations of many of these organizations in the CIS and SEE are generally ineffective. On the import side, they tend to delay shipments, sometimes extensively, sometimes intentionally. In the case of Ukraine, for example, the standards regime has been identified as an explicit NTB designed to selectively constrain import flows (World Bank 2004q). On the export side, standards organizations are not able to provide the information needed to exporters to ensure that the latter meet the requirements in export markets.¹² Assistance to these organizations has typically been offered by donors in connection with WTO accession. There is a continuing need for strengthening these institutions even after WTO accession has been secured (World Bank 2004d).

Transport

Transport costs are a major determinant of competitiveness, as the cost of international transport is often higher than the applicable tariff in external markets. Transport problems faced by these countries are both internal and external, related to the question of transit, which is a major issue discussed in chapter 5.

During the period of central planning, there was substantial investment in transport infrastructure. At the same time, the infrastructure was designed to service the trade flows established with and within the former Soviet Union. After independence, demand for transport services declined, *pari passu* with the substantial decline in economic activity. At the same time, existing infrastructure has been poorly maintained, and little new infrastructure has been added to address the needs for changing trade patterns; in addition, reform of the transport sector management and financing has been slow. As a consequence, in many of the countries in the Region, especially in SEE and the CIS, the transport infrastructure is a significant impediment to expanded trade. The many problems identified in various country studies include (a) freight charges that are frequently highly subsidized, resulting in poor financial condition of transport enterprises (which in many cases continue to be publicly owned); (b) the poor condition of the road infrastructure, as well as a trucking fleet that is aging and not being renewed; (c) antiquated rolling stock and lack of shunting stock and essential maintenance; and (d) limited airfreight services, which are useful only for the few high-value/low-weight exports of the Region's countries.

In addition to these problems, there are large costs resulting from corruption and unofficial payments (see chapter 4). For example, in the Caucasus, moving a generic containerized consignment by road from Northern Europe to Tbilisi—the Georgian leg—accounts for nearly 46 percent of total costs, with unofficial payments to border agencies, the road police, and other agencies representing more than 90 percent of the costs inside Georgia. Moving a similar consignment by road to Yerevan—the Caucasus leg—accounts for 67 percent of total costs, with unofficial payments accounting for almost half of total costs (World Bank 2002d; World Bank 2003c).

In many of the Region's countries, especially in the CIS and SEE, there is a need for substantial institutional strengthening of the various road funds and railway companies; there is also a need for substantial investment in maintenance and repair; there is a need for a reassessment of demand and supply for various transport services, in the light of the emerging pattern of economic activity and international trade; and there is a need for simplifying procedures, strengthening the border agencies, and eliminating corruption. Such improvements should be

viewed as an important component of any effort to strengthen the integration of these economies into world trade. For a more detailed discussion of transport costs and international integration, see chapter 5.

Transit Issues

As with other issues, there are distinctly different transit problems in Southeastern Europe, Central Asia, and the Caucasus. Moldova appears to face serious transit problems as a consequence of substantial delays on the border with Ukraine. In Central Asia, the problems are concentrated in the Kyrgyz Republic and Tajikistan, with each facing transit problems—in the former through Kazakhstan and in the latter through Uzbekistan. In both cases, the problems relate primarily to road transport and not to rail. Indeed, all Central Asian railways use the same rolling stock, track standards, and rule books, and there appears to be significant cooperation among the rail authorities in the three countries. In the Caucasus, the problems derive from the Armenia-Azerbaijan conflict and the Turkish blockade of Armenia, as described in box 3.5.

The Challenges Ahead

As suggested in chapter 2, the fundamental constraints limiting the trade performance of countries in the Region relate to weaknesses in their trade-related policies and behind-the-border institutions. The experience of these economies over the last 15 years suggests that liberal trade policies affecting imports are necessary but not sufficient for these countries' effective integration into the world economy. Also, most of these countries have done little to encourage, and have often discouraged, exports.

The main challenges they face, however, relate to other behind-the-border policies and institutions. Some of these factors, such as fostering greater competition, improving governance, and adhering to the rule of law, are intimately linked to more general improvements in economic management and the performance of market institutions (these issues are discussed in chapter 4). Others, such as strengthening of the customs service, improving standards and marketing organizations, overhauling the transport system, and facilitating trade and transit are directly linked to external trade (for more, see chapter 5).

To be sure, these problems have been identified in recent years (Michalopoulos 1999), and some countries in the Region have made progress in addressing them. Unfortunately, however, the increasing attention paid to these issues has not yet resulted in Region-wide improved performance. Much more needs to be done on a sustained basis in all of the countries before trade performance can improve. Part III of this study examines the behind-the-border impediments, institu-

BOX 3.5**Transit Problems in the CIS**

Kyrgyz Republic. The destination of a high percentage of the exports is Russia and the EU. Road transport costs are typically 10–15 percent of total costs, of which only about one-third are fuel costs. The remainder involves different kinds of fees and payments to be made officially and unofficially at various points in transit countries. The main problems arise in connection with transit through Kazakhstan.^a Many of these barriers are being addressed through an Agreement on Transit that started to be implemented in early 2004. However, some barriers are still in place, including various road taxes and fees imposed by local authorities, as well as harassment by local police, bureaucratic delays created to extract bribes, and weak capacity in customs administration (World Bank 2004d; see also Molnar and Ojala 2004). Transporters also complain that axle weight limitations are set differently and are biased against their trucks, and that slight deviations above weight limitations attract draconian penalties, which force them to carry inefficiently small loads (Cuthbertson and Jones 2000).

Tajikistan. The geographic location of Tajikistan is as difficult as it gets, and as a consequence, Tajik trade is burdened with one of the highest logistics costs in the world (World Bank 2004I). About 80 percent of Tajikistan's exports must be routed through Uzbekistan, in part because of the topography and in part because Tajikistan's northern and southern rail networks, which carry most of the exports, are not connected. At the same time, Uzbekistan depends on transit through Tajikistan for access to the Fergana Valley. Cooperation is working better on rail than on road traffic. In the latter case, Tajik drivers complain that current border fees are higher for exports than they are for imports, and that customs regulations are often complex and vague, leaving a great deal of leeway for harassment and bribery (World Bank 2004I). Also, Tajik truck drivers need a visa to enter Uzbekistan, and obtaining or renewing one can be problematic and time-consuming (World Bank 2004I).

tions, and policies in the Region in detail and provides suggestions for reform so as to make concerted, Region-wide progress on this front.

The international community also has responsibilities: the poorer countries in transition need technical and financial assistance to strengthen their trade-related institutions. The World Bank and other multilateral and bilateral donors have a number of assistance programs in place for this purpose, for example, to support customs reform, to improve trade-facilitation institutions, and to strengthen the overall country trade-related capacity to meet WTO-related commitments. However, although they share many of the characteristics, none of these countries formally qualify as "least developed countries" under the UN definition; this means that they cannot benefit from the many programs that the international community has

The Caucasus. Transport costs account for about 10 percent of the total value of merchandise in Armenia and slightly less in Azerbaijan and Georgia. They have been declining in recent periods, as there has been increased transit through Georgia and Iran. All countries levy high transit fees on foreign vehicles, but the fees appear to be substantially lower than those levied by the countries in Central Asia. Armenia has been the country most affected by the blockade, as it has to reroute its trade through Georgia. This has had a significant adverse effect on Armenia's exports. It is estimated that opening the Turkish border will halve the trucking costs between Armenia and Turkey. There would also be substantial savings if Turkish ports were used for transshipments of sea freight, and there would be significant, if somewhat lower, savings in freight costs to Iran. In addition to savings in money, the direct link between Armenian and Turkish road systems would increase the availability, predictability, and reliability of shipping services. By comparison, Azerbaijan transport costs would decrease only by about 10 percent as a consequence of opening up the road between Armenia and Turkey. Georgia, on the other hand, would lose transit fees if the blockade on Armenia were lifted. Nevertheless, as noted earlier, all of the countries would gain from the increased trade and growth that would result from the normalization of political relations (Polyakov 2001).

Moldova. Despite a free transit provision included in its FTAs with Russia and Ukraine, Moldova experiences serious problems with the transit of goods destined for Russia, its main market, through Ukraine. The transit environment remains chaotic, and a regime of free transit has never been achieved (World Bank 2004f).

Source: World Bank staff.

Note: a. See Cuthbertson and Jones 2000. While the ratio of transport costs to merchandise value for these countries is high, it does not come close to the problems faced by a developing country like Malawi, where the ratio of transport cost to merchandise value was as high as 50 percent (UNCTAD 2001).

organized to strengthen the trade-related capacity of certain countries (see box 3.6).

Global Integration

WTO Accession

All eight of the countries in the Region that have recently become members of the EU are WTO members. Only 9 of the other 19 countries in the Region have acceded to the WTO. Romania became a contracting party to the GATT in 1983 under a special protocol and despite serious concerns as to whether its commitments at that time, for example regarding tariffs, were meaningful in the context of

BOX 3.6**Least Developed Countries (LDCs) and Transition**

The official recognition of a country as “Least Developed” by the United Nations provides it with access to a number of assistance programs, as well as to preferential treatment in trade. To be added to the list, a country must meet a number of criteria based on a UN triennial review. In its latest review of the list of Least Developed Countries in 2003, the Economic and Social Council (ECOSOC) of the United Nations used the following three criteria for the identification of LDCs, as proposed by the Committee for Development Policy (CDP):

1. A low-income criterion, based on a three-year average estimate of the gross national income per capita (under \$750 for inclusion, above \$900 for graduation)
2. A human resource weakness criterion, involving a composite Augmented Physical Quality of Life Index (APQLI)
3. An economic vulnerability criterion, involving a composite Economic Vulnerability Index (EVI)

To be added to the list, a country must satisfy all three criteria. To qualify for graduation, a country must meet the thresholds for two of the three criteria in two consecutive triennial reviews by the CDP. Based on the CDP report, the ECOSOC makes recommendations to the General Assembly, which is responsible for the final decision on the list of LDCs.

As of 2004, 50 countries were designated as LDCs. None were transition economies, although some may have met at least two of the three criteria for inclusion. As a consequence, no transition economy could benefit from a number of international initiatives such as the Integrated Framework for Trade-Related Technical Assistance for LDCs, aimed to strengthen these countries’ institutional capacity and become better integrated into the world trading system.

Source: United Nations.

central planning. Subsequently, it renegotiated its GATT protocols and became a founding member of WTO. Bulgaria applied for admission to the GATT in the 1980s and eventually became a member of WTO in 1996. Albania, Armenia, Croatia, Georgia, the Kyrgyz Republic, FYR Macedonia, and Moldova became WTO members in the last five years. All remaining countries, with the exception of Turkmenistan, are in various stages of the accession process. Some, like Russia and the related application for accession of Kazakhstan, as well as Ukraine, are relatively advanced. Others lag behind (see table 3.5).¹³

WTO membership results in greater integration into world trade. Trade among WTO members is on average 25 percent higher than

TABLE 3.5
Timetable of Accessions to the WTO

Government	WP establishment	Memorandum	Tariff offers (latest)	Service offers (latest)	Draft working party report
Russian Fed.	06/93	03/94, 01/01	02/01	06/02	05/03
Belarus	10/93	01/96	03/98	—	—
Ukraine	12/93	07/94	03/02	07/03	09/04
Uzbekistán	12/94	09/98	—	—	—
Kazakhstan	02/96	09/96	04/01	05/03	—
Azerbaijan	07/97	04/99	03/03	04/03	—
Bosnia & Herzegovina	07/99	11/03	—	—	—
Serbia & Montenegro	01/01	06/02	—	—	—
Tajikistan	07/01	02/03	—	—	—

Source: WTO.

Note: — = not applicable.

trade among nonmembers (EBRD 2003). WTO membership is important for a number of reasons: first, because membership promotes the establishment of the legal framework and market-based institutions in support of international trade that were absent under central planning. Second, membership is important because it provides better guarantees for market access through the provision of unconditional MFN status—something that some transition economies do not enjoy in all markets—and through the avoidance of arbitrary measures that limit market access to nonmembers. Third, because the WTO has established a binding dispute settlement mechanism, which has proved effective in adjudicating trade disputes. This is especially important for a number of the smaller countries in transition, who have in the past been victims of their larger neighbors, who used trade measures as a weapon in settling a variety of economic disputes.

Relations with the EU

The eight transition economies in Eastern Europe that have recently become EU members—the EU-8—have accepted the EU *acquis* in its totality and are in the process of implementing the myriad new obligations that come with membership. Included in these new obligations is the adoption of the common EU external tariff and all of the EU regulations governing external trade, including the preferential agreements the EU has signed with many countries worldwide. These countries have had to abandon all of the bilateral preferential agreements they had signed with other countries in the Region and all of their own trade protection immediately upon accession, with the exception of a short transition period for a few Polish products. Undoubtedly, EU accession will have a profound, and in the long

term, positive impact on their economies. It will also have both a short-term and a longer-term impact on the remaining economies in transition.

The biggest challenge for transition countries in Southeastern Europe is posed by their own future membership and integration with the EU. With few exceptions, these countries have already signed Association Agreements—which involve free trade arrangements in many sectors and preferential treatment in others—with the EU. Bulgaria and Romania are in advanced stages of negotiations for EU accession, and Croatia has been approved as a candidate country. FYR Macedonia has signed, and Albania is well along in the process of negotiating a Stabilization and Association Agreement (SAA) with the EU, which envisages both free trade arrangements and an alignment of their policies to those of the EU, with a view to their future accession. Bosnia and Herzegovina and Serbia and Montenegro are also engaging in consultations with a view to signing similar agreements with the EU. The bulk of these countries' imports (more than 70 percent) are covered by preferential European arrangements, and a significant portion of the remainder involve energy and raw materials, which are not protected by the EU. Indeed, with the possible exception of the LDCs, these countries seem to occupy the top of the EU preference pyramid (Stevens et al. 1999). The average tariff on their imports to the EU (weighted or unweighted) is less than half of that applied by the EU on imports from the CIS (EBRD 2003, table 4.3).

At present, MFN tariffs on industrial products in all of these countries are substantially different—usually higher—than those of the EU. Because they already have or will have free trade arrangements with the EU that would cover most, if not all, industrial products, the current situation results in significant trade diversion that yields high rents to EU producers but no benefits to these countries (Kaminski and La Rocha 2003a). These countries would be better off by progressively realigning their overall MFN tariff schedule to that of the EU, even in advance of EU accession. However, the EU tariff will itself likely be changing as a consequence of the WTO multilateral trade negotiations. The transition economies of SEE would need to coordinate their position on the multilateral trade negotiations with the EU, but they can also use these negotiations as a means of making further adjustments to their tariff schedule so that it can be aligned to that of the EU at the earliest possible opportunity.

EU membership would require the realignment of a vast number of other policies and institutions and give rise to a large and complex set of social and economic adjustment issues, which would include, but not be limited to, trade. It is a huge task that is currently occupy-

ing a large number of policy makers and analysts both in the EU and in the countries themselves.

The EU relationship with the CIS members is fundamentally different. In most cases, the relationship is governed by so called “Partnership and Cooperation Agreements” (PCAs), which are in force with all CIS countries except Belarus, Tajikistan, and Turkmenistan. The PCAs are basic commercial treaties. The major benefits afforded by these treaties are the provision of MFN and, in some cases, GSP (Generalized System of Preferences) treatment and adherence to basic commercial rules and practices. These treaties have been especially important for the transition economies while they have not been WTO members. Once they become WTO members, the mutual commitments undertaken in the context of accession far exceed anything contained in the PCAs. It is for this reason, for example, that Russia’s negotiations with the EU over pricing of natural gas in the context of WTO accession have been so protracted and difficult.

The benefits derived from EU preferences under the GSP have been modest. In Ukraine, it is estimated that roughly 30 percent of total Ukrainian exports are eligible for GSP coverage. Of the total eligible for coverage, roughly 50 percent of imports actually received preferential treatment. In Moldova, the eligibility and utilization rates were slightly higher. However, Moldova’s main export, wine, was not included (World Bank 2004f). These results are in line with the results obtained under EU’s GSP by other countries. The benefits are modest because (a) the commodity coverage under the GSP is limited; (b) competing countries enjoy deeper margins of preference—for example, the average EU tariff on ethyl alcohol is 30 percentage points lower than what exporters from Russia and Ukraine face; and (c) utilization is limited, in part because of lack of information in the countries themselves and also because adhering to the GSP provisions regarding rules of origin is quite difficult, especially for small and medium enterprises (World Bank 2004i; World Bank 2004q).

It should be underscored that, as most of CIS exports to Organisation for Economic Co-operation and Development (OECD) markets consist of energy and raw materials, which are not significantly protected, market access conditions have not resulted in major constraints to overall export performance. There are significant problems, however, in specific export sectors, for example, metals, textiles, chemicals, and processed food, many of which have been the targets of antidumping and other protection in EU and other OECD markets.

A number of CIS members, notably Moldova, Ukraine, and some of the Caucasus countries, aspire to some type of closer association with the EU. Moldova, for example, has stated that it would wish to

be included in the SAA process; Ukraine is considering how to associate itself with the EU. It is unclear at this stage how far the EU is willing to go in strengthening its economic links with these countries. It appears that the future economic relationships of these countries with the EU will depend a great deal on political and human rights issues, and less on strictly economic questions.

EU Enlargement

The EU enlargement will have profound effects not only on the economies in the Region who already have become EU members but also on countries in the Region who are not in the EU, especially those in the CIS who have no preferential arrangements with the EU. The effects are likely to be different in manufacturing from those in agriculture.

In manufacturing, EU enlargement is likely to have positive short-term effects on CIS countries. They will have relatively little change in access to the EU-15 markets, as the enlargement countries already have duty-free access in these markets. On the other hand, market access in the enlargement countries themselves will improve, as these countries (for example, Poland and Hungary), have tariffs that are much higher than the EU common external tariff (World Bank 2004f; World Bank 2004q). For countries in SEE, the situation regarding exports of manufactures is also likely to change little. These countries already enjoy very free access to the EU-15 markets. Access to the enlargement country markets has also been relatively free as a result of the membership of some of the SEE countries in the Central Europe Free Trade Agreement (CEFTA). For the Western Balkan countries that were not members of CEFTA (Albania, Bosnia and Herzegovina, FYR Macedonia, and Serbia and Montenegro), the enlargement will mean definitive improvement in market access.

The situation in agriculture will be very different. To begin with, existing EU agricultural policies under the Common Agricultural Policy (CAP) cause significant difficulties to both CIS and SEE agricultural development. These policies involve substantial production supports and export subsidies of products by other countries in the Region that these countries cannot match. Enlargement will have two negative short-term effects on these economies' agriculture: first, countries like Poland and Hungary, which are competitors to the SEE and CIS economies, will enjoy far better access to the markets of the EU-15 for agricultural products; second, the enlargement countries will benefit from EU supports and subsidies, thus making them stronger competitors in the SEE and CIS countries' own markets.

Against these negative effects, it is possible that market access in some enlargement countries, and for some products, will improve because protection in their own markets had been greater than EU protection. However, the net overall short-term effect in agriculture is likely to be negative.

In the longer term, however, EU enlargement is likely to have a net positive effect on the CIS and SEE countries. The short-term positive effect on manufacturing exports will be augmented by the dynamic effects that EU accession will likely have on the enlargement countries. In agriculture, EU supports could well decline as a result of internal budgetary constraints; at the same time, international pressure arising in the context of the Doha multilateral trade negotiations also may have salutary effects.

“Market” or “Nonmarket” Economies?

One of the most serious market-access problems the SEE and CIS countries face in virtually all markets globally is that their exports are frequently the target of antidumping actions by both developed and developing countries. In part, this is because many are not members of the WTO. In part, however, it also is because so many of these countries have been designated as “nonmarket economies” (NMEs) for purposes of antidumping cases by developed countries, such as the EU and the United States. It also arises in the case of the EU for the imposition of safeguards against SEE and CIS exports. The NME designation involves the use of different, less-demanding, and less-transparent procedures for the complainant countries in the determination of dumping and, in the case of the EU, also in the use of safeguards against imports from the NME. It results in more easy “findings” of dumping or the establishment of “price undertakings” that involve the cartelization of markets.

Since the establishment of the WTO in 1995, the Region’s countries have been the target of 325 antidumping actions, or 13.5 percent of total antidumping actions worldwide.¹⁴ This is much higher than their share in world trade. The bulk of the actions have been taken against Russia and Ukraine (86 and 51 antidumping investigations, respectively [see annex table 3.3]). Actions against the EU-8 have been less frequent relative to their share in world trade (see table 3.6) than have actions against countries in SEE, many of whom are not WTO members. Ukraine has the distinction of having a higher share of antidumping actions relative to its exports than any other country worldwide, including China. Russia’s share is also large, especially if one considers that a large share of Russian

TABLE 3.6

Antidumping: Share of Affected Economies in Total Cases Relative to Share in World Exports in Percentages and Ratios

Affected economies	World exports 1995–2003		Total antidumping investigations 1995–2003			Definitive measures 1995–2003	
	Exports (\$ billions)	Wld. export share (%)	No. of cases	Share (%)	AD share/ Wld. exp. share	DM share (%)	DM share/ Wld. exp. share
World	53,322	100.0	2,416	100.0	1.0	100.0	1.0
Industrial countries	34,541	64.8	683	28.3	0.4	25.4	0.4
Developing countries	16,354	30.7	1,408	58.3	1.9	58.0	1.9
All transition countries	2,427	4.6	325	13.5	3.0	16.6	3.6
Non-WTO members (10)	1,160	2.2	177	7.3	3.4	9.7	4.5
Nonmarket countries (7)	141	0.3	15	0.6	2.3	0.7	2.5
Nonmarket countries (18)	3,299	6.2	481	19.9	3.2	27.0	4.4
All Region	2,427	4.6	325	13.5	3.0	16.6	3.6
EU-8	1,058	2.0	90	3.7	1.9	3.0	1.5
CIS	1,161	2.2	175	7.2	3.3	9.9	4.6
SEE	214	0.4	63	2.6	6.5	3.1	7.8
Russian Fed.	815	1.5	86	3.6	2.3	4.7	3.1
Ukraine	141	0.3	51	2.1	8.0	3.1	11.8
China	2,142	4.0	356	14.7	3.7	16.8	4.2

Sources: WTO antidumping files and IMF Direction of Trade Statistics.

Note:

Non-WTO members include Azerbaijan, Belarus, Bosnia and Herzegovina, Kazakhstan, Russia, Serbia and Montenegro, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan.

Nonmarket (7) includes Azerbaijan, Belarus, Cuba, Democratic People's Republic of Korea, Tajikistan, Turkmenistan, and Uzbekistan. Nonmarket (18) includes above nonmarket 7 countries plus Albania, Armenia, China, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, Mongolia, Russia, Ukraine, and Vietnam. Moldova is included both in the CIS and in the SEE.

trade is in raw materials and fuels, which are not the subject of antidumping actions. Actions against these economies are more likely, as a general rule, to move beyond investigations and lead to the actual undertaking of definitive antidumping measures or price undertakings.¹⁵

The main sectors targeted have been ferrous and nonferrous metals and chemicals, including fertilizers. It is difficult to assess the impact of the antidumping actions on particular sectors of the economies affected. In Ukraine, at present, there are 25 tariff lines affected by EU AD restraints (World Bank 2004q). Although the overall volume of these exports is small relative to total Ukrainian exports to the EU, this is not to suggest that these measures have not had a significant restraining effect on Ukrainian exports: in some cases, Ukrainian exports simply ceased after the AD actions had been introduced; in

others, they grew, but it is unclear by how much more they would have grown without the restraining effect of antidumping.

Designation of a country as a nonmarket economy makes it easier to obtain a finding of dumping because the procedures used are more arbitrary and less transparent. Such designations were started in the 1980s in order to take into account the price distortions inherent in central planning. They are still used today by the United States and the EU and other OECD countries, even in cases where central planning practices have long disappeared in the targeted economies.

When an antidumping investigation is initiated against an NME, the costs and exchange rates of a “surrogate” or “analogue” country are used for the determination of a “normal” value, against which the actual price is measured; this is because it is assumed that prices and exchange rates in centrally planned economies did not reflect true opportunity costs. This introduces the possibility for arbitrariness and nontransparency. Equally, these procedures make it easier to induce exporters to agree to minimum price undertakings such as those concluded with Russia on uranium and aluminum (Michalopoulos and Winters 1997), which involve the cartelization of the market in specific products.

With regard to antidumping, the WTO provides legal justification for such practices through the reference of Article 2.7 of the Antidumping Agreement to the second Supplementary Provision to paragraph 1 of Article VI in Annex I to GATT 1994, which permits such different treatment “in the case of imports from a country which has complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the State” (Palmer 1998). These practices perhaps were fully justified when virtually all trade was controlled by state trading enterprises or ministries under central planning, and prices were fixed by the state and hence could not be taken to reflect “normal value.” Many—but not all—of the Region’s countries have made great progress in introducing market forces and eliminating state trading in recent years. It would be very difficult to argue that, for example, Ukraine or even Tajikistan at present has “a substantially complete monopoly on trade” or that all domestic prices are fixed by the state.

The EU distinguishes among three groups of countries for antidumping and safeguard purposes: (a) “nonmarket economies,” which currently includes Azerbaijan, Belarus, Tajikistan, Turkmenistan, and Uzbekistan in the Region (as well as Cuba and the Democratic People’s Republic of Korea outside the Region), none of whom are WTO members; (b) a second group of “transition economies,” which includes Albania, Armenia, Georgia, Kazakhstan,

the Kyrgyz Republic, Moldova, and Ukraine in the Region (as well as China, Mongolia, and Vietnam outside the Region); and (c) all other countries that are considered “market economies.”

For the EU’s nonmarket economies (group [a] above), a single antidumping margin is calculated for the whole country, using data from a third country that is a market economy. In the context of the second group, companies in these countries can be granted “Market Economy Treatment” (MET) on a case-by-case basis. However, the onus is on the countries to demonstrate that they operate under normal market conditions. Otherwise, such companies are treated as operating in NMEs and are subjected to the more arbitrary and less transparent “analogue” country treatment. A country listed in the first group can move to the second group if it becomes a member of the WTO. However, Russia is treated as a market economy, although it is not a member of the WTO; equally Kazakhstan, Ukraine, and Vietnam are in group (b) although they are not WTO members. In the context of safeguards, the EU standards for taking action against nonmarket economies are lower than they are for other countries that are WTO members. In the case of nonmarket economies, merely the coexistence of higher imports and injury to domestic producers—as opposed to a causal link—needs to be demonstrated, and there is no limit on the duration of the action, as required by GATT article XIX (Michalopoulos and Winters 1997).

In the United States, there is no formal NME list, and decisions are made on a case-by-case basis, usually involving the same taxonomy as utilized by the EU.

The continued designation of countries that are members of the WTO as NMEs is a serious problem that results in arbitrary, nontransparent, and discriminatory treatment of their exports relative to other countries with similar economic management. It is unclear, for example, under what standards EU classifies Bosnia and Herzegovina and Russia as “market economies,” while it classifies Albania and Ukraine as “economies in transition.” Similarly, it would appear that “economies in transition” includes both countries like Ukraine and Vietnam, who are not WTO members, and others, such as Albania, whose economies have been vetted extensively in terms of the degree of privatization they have achieved.

WTO membership would address the problem that nonmarket economies have regarding the different standards imposed by the EU on safeguards. WTO membership, however, would not automatically terminate the designation of countries as nonmarket economies nor completely terminate the problems they have with antidumping; however, it might help. Membership could inhibit the most egregious excesses in antidumping practices against which a nonmember has

no recourse, as the WTO dispute settlement mechanism—albeit with some limitations—can be utilized for this purpose. More generally, the standards of accession have evolved in such a way as to provide members with assurances that a newly acceding country is fundamentally run on market principles, making current antidumping practices, if not illegal, demonstrably unfair. It can be reasonably assumed that countries in the Region would not secure WTO membership unless they could demonstrate that their trade was fundamentally based on market transactions. Thus, in principle, WTO membership undoubtedly would tend to create pressure to terminate the nonmarket designation in national practices of antidumping and permit all WTO members to be treated the same in major markets.

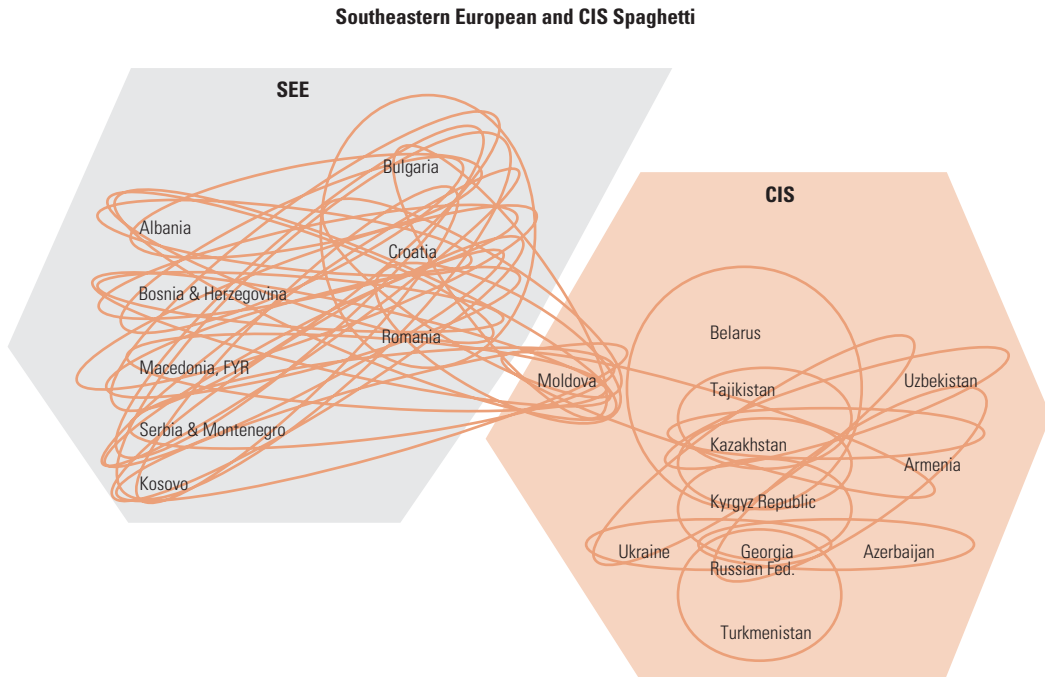
Unfortunately, this has not happened so far, and some WTO members continue to be subjected to NME designation on a case-by-case basis. Others are designated as NMEs even though there is no evidence that their economies are subject to central planning controls in any major way. Rationalizing the treatment of economies in the Region, especially WTO members, in the context of antidumping actions, would appear to be an important priority for the international community and would help improve the Region's economies' access to major developed-country markets.

Regional Trading Arrangements

All of the countries in the Region participate in one or more regional trade agreements (RTAs). The multiplicity of these RTAs has been likened to a “spaghetti bowl” (see figure 3.1). Among the Region's countries, those in Southeastern Europe and the CIS members are particularly active in a large number of regional cooperation agreements having potential impact on trade. While some of the challenges of regional integration in these two groups of countries are similar, many are not, and there is one country—Moldova—which straddles both groups; this itself poses unique problems (see box 3.7).

In SEE, the regional cooperation effort is underpinned by the development of an institutional framework formed by the countries of the region within the Stability Pact for Southeast Europe. This has led to the signing of a Memorandum of Understanding (MOU) on Trade Liberalization and Facilitation in 2001, which is playing a major role in promoting regional cooperation efforts among all eight countries and Kosovo.¹⁶ Under the terms of the MOU, the countries have established a network of 28 bilateral free trade agreements. The main challenge they face is how to move forward and establish a single free trade area, as well as how to move beyond regional trade liberaliza-

FIGURE 3.1
The Myriad of Regional Trade Agreements Resembles Spaghetti Bowls



tion to cooperation in other areas, such as liberalizing services and aligning trade-related policies and institutions to those of the EU.

In the CIS, the main problem is that implementation lags far behind the ambitious formal commitments on trade cooperation made at the highest level by participating governments. Both the CIS-wide Free Trade area, and the Eurasian Economic Community (Evrazes), which involves Belarus, Kazakhstan, the Kyrgyz Republic, Russia, and Tajikistan,

BOX 3.7

Moldova’s Free Trade Arrangements

Moldova deserves separate mention in the context of regional integration because it has its foot in two subregions: it has bilateral preferential arrangements with Russia and Ukraine and has been granted “observer” status in Evrazes, whose aim is to establish a customs union among its members. At the same time, it has negotiated or signed seven bilateral FTAs with countries in SEE under Memoranda of Understanding on Trade Liberalization of the Stability Pact. Moldova can continue its FTAs with other CIS members, but it clearly cannot be a member of a customs union with Russia and others in the CIS (meaning it cannot have the same external tariff) while entering into FTAs with the Balkan countries.

amount in practice to far less than their names would lead one to believe. An issue that is common to both SEE and CIS is the form of regional trade liberalization: should it involve the establishment of free trade areas or is the establishment of one or more customs unions preferable?

Regional Integration in Southeastern Europe

Efforts at regional economic integration in SEE have been strongly promoted by the OECD countries and multilateral financial institutions, initially as a means of promoting regional political stability and later because regional trade came increasingly to be seen as one of the many elements needed to stimulate growth in some of the war-torn economies of the region. The EU also promoted regional trade through the SAA process, which explicitly links liberalization of trade with Europe to regional cooperation and liberalization among the countries in the region.¹⁷ The regional cooperation effort in turn was underpinned by the development of an institutional framework in the form of a Working Group on Trade Liberalization and Facilitation established by the Stability Pact, in which all countries in the region and Kosovo, as well as developed countries and multilateral institutions, participate. The Working Group has been quite active, both in providing a setting within which agreements on regional cooperation such as the MOU can be negotiated and in monitoring their subsequent implementation.

The MOU contains commitments in a large number of areas:

- It commits countries to reach agreements to establish FTAs with each other, and it lays down standards for product coverage both for existing and future FTAs among the participating countries as well for the rules of origin they use in the FTAs.
- It commits the countries to a standstill on any measures that would adversely affect trade and to monitoring nontariff measures that impede trade.
- It recognizes the importance of liberalizing trade toward third countries.
- It invites countries to deepen their trade liberalization with each other through further opening up of their trade in services.
- Finally, it commits countries to take steps to harmonize their legislation and regulations on a number of trade-related topics, such as competition, investment, and standards and to bring them more in line with those of the EU.

Progress in implementing the MOU provisions concerning the conclusion of FTAs among the countries in the Region has been impres-

sive. All of the bilateral free trade agreements envisaged by the MOU have been signed and are under implementation (annex table 3.4). Also, most agreements have met the “quality” standards regarding product coverage measured both in terms of trade volume and liberalized tariff lines agreed to under the MOU. The exceptions have been the result of limited liberalization in agriculture. Even here, however, the countries have committed themselves to take actions in the near term to ensure that the “quality standards” of the FTAs are met.¹⁸

There is no evidence of increased trade restrictions of a nontariff nature in SEE. However, there is increasing realization that, despite efforts at improving border crossings, simplifying procedures, and customs reform, serious problems in trade facilitation continue to plague regional and global trade.¹⁹

At the same time, one should not exaggerate the importance of the FTAs as a stimulus for trade and overall growth in SEE. Trade links among several of the countries in SEE are very small. Even if substantial growth in regional trade among them occurs, as is already happening, present trade volumes are so small that little overall effect on growth is likely to materialize.

Looking to the future, there are two key issues faced by the countries of SEE in regional integration. First is how to move forward in cooperation in other areas beyond regional trade in goods. The MOU covers much more than FTAs, but progress in such areas as services has proved slow, in part because of limited institutional development at the national level in the services sectors themselves.

The other issue has to do with the form of future trade relationships among these countries. Having a large number of bilateral FTAs—each with a different set of bilateral exemptions, even though they cover a small component of trade in each agreement—undermines the notion that a “virtual” unified FTA has been achieved throughout the Balkan economic space. The bilateral FTAs should be seen as an important step in the integration process, but not as an end in themselves. Implementing these agreements is important, but maintaining these agreements as they are may not be in the long-term interests of the countries that have signed them: the benefits in terms of trade creation are likely to be small and the dangers of distortions and corruption are high (Kaminski and de la Rocha 2003a). The more complex the system, the less transparent it is and the greater the opportunity for trade deflection, corruption, and distortions, especially when the trade-related institutions that have to implement the policies, such as customs and border crossings police, are as weak as they are in the countries of the Region. Thus, there is little doubt that the countries should start thinking about moving on to deepen their integration (see box 3.8).

BOX 3.8**Harmonization of FTAs in Southeastern Europe: The Options Ahead**

Over a period of three years, the countries of SEE, plus Moldova, have finalized a network of 28 bilateral FTAs, a remarkable achievement. In November 2003, at the Rome Ministerial Meeting, the Stability Pact Working Group on Trade, within which the agreements were negotiated, was asked to come up with options for the next step, that is, “how best to harmonize the bilateral free trade agreements with each other in order to improve the transparency of the network of bilateral free trade agreements and its efficient administration” (2003 Rome Ministerial Statement). Harmonization makes sense only if it brings net benefits to firms—minimizing their operating costs and enlarging the market size covered by a unique FTA. Five options or suboptions have been identified and are discussed below.

Option 1. A Trade Working Group (TWG) with an Expanded Mandate

The first option would be to keep unchanged the current FTA texts and to minimize the costs of operating a web of 28 FTAs by expanding the role of the TWG. An expanded TWG could tackle the implementing rules by being conceived as the “Joint Committee” of all the FTAs. This role does not require eliminating the bilateral Joint Committees, which could remain the “first instance” bodies, with the TWG playing the role of an “appeal” body. In this context, the TWG could have two important roles. First, it could be in charge of the monitoring exercise following the implementation of the liberalization process specified by the FTAs, providing the necessary interpretations of the treaties in case of doubt, and possibly even playing the role of a dispute settlement mechanism for the signatories. Second, the TWG could ensure the consistency of the implementation of the various FTAs once the liberalization is achieved. If one wants the web of 28 FTAs to work smoothly, instruments of contingent protection defined in the FTAs (sometimes in quite different terms) require relatively similar domestic regulations, and—more important—a relatively similar way to enforce these regulations by the domestic institutions. An expanded TWG could play a useful role in this context.

Viewed from a technical point of view, this first (minimal) option would provide small benefits, but it would also entail small costs, which arises from the fact that an expanded TWG would require very limited institution building, and it could be quickly implemented and progressively expanded, as the demand for its services grew. An expanded TWG would simply need to meet more frequently and would probably need to include representatives from the FTA-related domestic institutions, such as offices in charge of implementing contingent protection. However, its expected benefits are also likely to be limited because, ultimately, an expanded TWG would be constrained by the existing FTA texts.

Option 2. An Expanded CEFTA

The second option to consider would be to expand the geographical coverage of the CEFTA text to the whole Region. However, most—but not all—of the FTAs have most—but not all—of the CEFTA provisions. This feature has two implications.

(Box continues on the following page.)

BOX 3.8 (continued)

First, the CEFTA solution would not be very costly for the three countries that have already used the CEFTA text between themselves (Bulgaria, Croatia, and Romania) and the fourth, FYR Macedonia, which is discussion about membership. And some of these countries would join the EC in a few years. As a result, the CEFTA solution would result in small costs. However, it also would provide small benefits to these countries: they would shift to another type of trade agreement between them and with the rest of the Region—the one imposed by the *acquis communautaire*.

Second, the CEFTA solution would undoubtedly be more costly for the other countries of the Region. They would have to shift from their existing FTAs to a new treaty (CEFTA) that does not really exist in their legal trade regime. The benefits of such a shift are limited because CEFTA is a treaty with deficient provisions on some traditional trade issues and no provisions on the new trade issues, such as services or public procurement, essential for the growth of the Region's economies.

In sum, the cost-benefit balance of a shift to CEFTA is probably positive, but only in a small and transitory way. It may be slightly positive only if one also makes the assumption that there would be small political costs for shifting to a new text—for the current signatories, because the economic soundness of key CEFTA provisions is doubtful.

Option 3. A SEEFTA

The third option is to fully face the challenge generated by the tensions between a complex web of 28 FTAs and the potential outcome within reach—a potentially effective regional FTA. If there are political costs to harmonizing the existing FTAs, then they should be counterbalanced by the largest possible economic gains. This option does not require that all countries in the Region choose it. It is possible that countries that are well advanced in the EC accession process would find it more suitable to keep their existing agreements, while the others go ahead. The decision in this respect would presumably depend on how quick and how deep are the changes being introduced. There are three suboptions in this respect, none of which require a unique “consolidated” text, as each could be provided by separate but harmonized texts, though obviously this second possibility might add unnecessary and undesirable complexity to an endeavor aiming at simplification.

A free trade area for SEE is one such option. How to do it is one of the key challenges for the countries concerned. The trade architecture in Southeastern Europe is changing. Many CEFTA members became members of the EU, while FYR Macedonia has been accepted for CEFTA membership by the remaining three countries (Bulgaria, Croatia, and Romania). In terms of the future, one could visualize either an expansion of CEFTA or a new integrated FTA that includes all of the countries that signed the MOU. What will be done in that regard is in large part a political issue. On the economic side, CEFTA

Suboption 3a. The first suboption can be characterized as a “minimal classical SEEFTA”: classical because it deals only with trade in goods, and minimal because it does not go further than mere harmonization, aligning on the best available text. This limited objective confines the harmonization exercise to two crucial, from a business perspective, aspects of the existing FTAs’ “General Provisions”: competition rules and disciplines on contingent protection.

Suboption 3b. The second suboption can be characterized as a “maximal classical SEEFTA”: classical because, again, it deals only with trade in goods, but maximal because it deals not only with the inconsistencies, but also with many of the serious concerns arising from the weaknesses of the existing agreements. It would do so by putting the intra-SEEFTA trade under more economically sound rules, like the ones governing intra-EC trade, on issues such as competition and state aid. Rules on contingent protection would also be harmonized in a more economically sound way—again, to the extent that they involve intra-SEEFTA trade. For instance, the provision on structural adjustment could be harmonized and improved by the creation of a plurilateral mechanism for monitoring the measures taken, as in the case of Article 115 of the Treaty of Rome. Similarly, one should consider the elimination of the provisions on reexports and balance of payment difficulties that refer to approaches well regarded in a faraway past, but which have proven their inefficiency since then.

Suboption 3c. The third suboption can be characterized as a “modern SEEFTA”: modern because would shift the focus of the FTAs to the emerging core of trade relations (that is, services, public procurement, intellectual property rights, and so forth). Here, the scope of harmonization and thus the improvement are immense. As a result, the SEEFTA text could simply announce a few principles. The two most important principles, particularly in the EC context, are the mutual recognition principle and the country of origin principle. By adopting these two principles, a modern SEEFTA would put the Region on the same track as the EC, hence facilitating countries’ progressive integration into the EC services, technology, and public procurement markets.

Source: Messerlin and Miroudout 2004

covers a wider area of commitments than the MOU, but the quality standards for the free trade area under CEFTA are less demanding than those of the MOU. However, in both respects the differences are not great. The other question is whether a future SEE-wide preferential arrangement should be in the form of an FTA or a customs union.

Regional Integration in the CIS

Soon after the breakup of the Soviet Union, the CIS members established a CIS-wide FTA. A plurilateral agreement to establish a Free

Trade Area was signed by all CIS members except Turkmenistan in 1994. However, the original framework agreement was never ratified by the Russian parliament and therefore remains inoperative. Over the last decade, however, a patchwork of bilateral free trade agreements linking most CIS members has been signed. Subsequently, Belarus, Kazakhstan, the Kyrgyz Republic, and Russia agreed to establish a customs union. Tajikistan joined the agreement in 1999.²⁰ The latest development is the agreement among all of these countries as well as Ukraine to establish an Economic Union. There are also other agreements with a regional focus (for example, the Central Asian Cooperation Organization, consisting of Kazakhstan, the Kyrgyz Republic, Tajikistan, and Uzbekistan), and there is one agreement—TRACECA—that is a project to develop a transit corridor between Central Asia and the Caucasus.

The bilateral FTAs stipulate free trade in all goods between participating countries, but each has different product coverage and exemptions, as well as rules of implementation, such as the use of safeguards and quantitative restraints. As a consequence, at present there is a complex network of bilateral agreements among various countries whose coverage and rules change frequently and whose impact is very difficult to evaluate. A few products (for example, alcohol and tobacco) are excluded from all agreements. Efforts to establish a standardized list of exemptions have so far failed, however. Exemptions can be imposed unilaterally and are supposed to be accompanied by a schedule for their termination. However, these schedules are often not followed, and there appear to be no penalties for slippages. While the exemptions are concentrated on a few products, their trade restrictiveness appears to be high (World Bank 2004p).

The web of agreements hampers transparency and consistent implementation. For example, Armenia, the Kyrgyz Republic, and Moldova do not levy tariffs on goods imported from most of the other CIS countries on a reciprocal basis. On the other hand, Tajikistan gives preferential treatment only to the members of the Eurasian Economic Community and applies tariffs on goods imported from the others. Uzbekistan has bilateral free trade agreements with Azerbaijan and the Kyrgyz Republic. Georgia has bilateral FTAs with Azerbaijan and Armenia (but does not report having one with Uzbekistan, which the latter says it signed in 1996). In Azerbaijan, imports from Russia are subject to tariffs and the VAT; imports from Georgia and Ukraine to VAT only; and imports from Moldova to import tariffs only.

Contingent protection measures are a feature in all agreements and have been used extensively in Russia's relationship with Ukraine, based on procedures that have little transparency and appear to be

inconsistent with WTO provisions. The reciprocal retaliatory measures introduced by both countries against each other's trade have resulted in damage to both economies.

To operate an effective FTA, it is necessary to implement rules of origin, which is the responsibility of customs authorities. Given the extreme weakness in the customs institutions in all of the countries in the CIS, the porous borders, and the complex character of the agreements, the actual tariffs paid on any product to any authority on intra-CIS trade is a very chancy thing that has little to do with the formal agreements signed by the countries between which trade is occurring. Moreover, in the absence of a plurilateral dispute settlement mechanism, all disputes have to be resolved politically at the bilateral level. This is especially disadvantageous for small countries participating in these agreements.

The Eurasian Economic Community is supposed to be a customs union. Its main driving force has been the traditional exporters in Russia, who have wanted to maintain their preferences and links to the traditional industrial structures in the other countries.²¹ At present, there is free trade among the participating countries, but their external tariffs diverge substantially, which means they have in place a free trade area, not a customs union.

The plans are to set up a customs union with a common external tariff by 2006. Russia expects the other countries to move to the Russian tariff. It is reported that progress on "harmonization" of the external tariff (which means convergence to the Russian tariff) is as follows. Between Russia and Belarus, approximately 95 percent of tariff lines have been harmonized; between Russia and Kazakhstan, approximately 85 percent; Russia and the Kyrgyz Republic, 14 percent; and Russia and Tajikistan, 60 percent. While these figures clearly reflect the dominance of Russia in this grouping, there is no information on the degree of divergence among the tariffs of the other countries.

FTA or Customs Union

Both in the CIS and in SEE, a major policy issue for future regional integration is whether the countries should aim to establish a customs union or aim to create or a maintain a free trade area. In the SEE, this issue has been raised primarily in academic circles (Kaminski and de la Rocha 2003a). In the CIS, it is of very important current policy interest because of Russia's continued efforts to forge such an arrangement with a number of CIS members. The basic difference between a customs union and a free trade area is that in a customs union all participating countries adopt a common external tariff, while eliminating all trade barriers among themselves. In a free trade area, countries retain

their individual tariffs toward third countries, while liberalizing toward each other.

A customs union has some obvious advantages from an economic standpoint: it does away with the problem of determining rules of origin for each of the participating countries, and it reduces the chances of corruption in customs, a problem in many transition economies. It also involves a deeper form of integration requiring further coordination of policies, for example, in allocating the proceeds from collecting the common tariff. It is likely to involve fewer product exemptions than an FTA, hence increasing the opportunities for trade creation through competition with more efficient firms in the participating countries. And, depending on where the common external tariff of the customs union is set, it may lead to both less trade diversion and to higher short-term costs because of the need for domestic firms to adjust to increased competition.

A free trade area makes it easier to tailor the pace of regional integration to the needs of individual countries by not requiring the adoption of a common external tariff, which may result in increased competition both from within the union (which the FTA would also create) and the rest of the world. At the same time, operating FTAs with a large number of different countries increases the complexity of the tariff regime and makes implementation difficult because of the need to implement rules of origin. Advocates of customs unions favor them precisely because they are likely to result in greater competition and tend to downplay the adjustment costs such competition could engender.

Establishing a customs union among SEE countries whose external tariff approximates that of the EU would introduce more wide-ranging liberalization, especially in manufactures, and aim at preparing these countries toward rapid integration (and adjustment) to world prices and competition, as well EU accession. On the other hand, an FTA with the EU, which, as envisaged in the SAAs, could take as long as 10 years to complete, would expose countries slowly but surely to very substantial competition from EU firms that are frequently already their main suppliers. This has a twofold implication: first, the FTA with the EU is not likely to result in significant trade diversion costs for SEE countries, as the EU may already be the low-cost supplier. Second, establishing a customs union among the SEE whose external tariff moves over the same period to approximate the EU external tariff is not likely to lead to significant increases in competition from firms in the rest of the world (and hence more adjustment costs), but it would tend to reduce the rents (excess profits) that would be obtained by EU firms in SEE markets by reducing the margin of preferences that EU firms enjoy.

Some of the same economic arguments apply to the question of whether the SEE should seek to conclude a customs union with the EU: an FTA tends to permit greater flexibility and a slower and more narrow integration, with exemptions (that is, greater protection) and competition tailored to individual country circumstances. In the case of a customs union with the EU, there is one additional consideration: the EU is a major international market where entry is frequently on a preferential basis. If the SEE countries were to establish a customs union with the EU, they would have to provide all of the preferences the EU extends to a very large number of developing countries under the Cotonou agreement, the Mediterranean agreements, and others. These preferences could result in even greater competition and adjustment costs in the SEE countries' own domestic markets. It is for these reasons, as well as the fact that FTAs such as CEFTA have also worked well for member countries as a stepping stone toward integration with the EU, that the European Commission tends to favor FTAs rather than customs union agreements as vehicles for future integration in the European Union. Their argument can be summarized as follows: a customs union for the SEE with the EU would tend to result in the SEE countries incurring the bulk of the economic costs of adjustment but few of the benefits of integration with the EU.

On the political side, countries will face difficulties in making the more far-reaching commitments required by a customs union than a free trade area. Their governments showed remarkable commitment to Regional goals by reaching speedy agreement on the bilateral FTAs. However, the differences in the level of development among them are substantial and have resulted, for example, in Bosnia and Herzegovina obtaining asymmetrical treatment in the bilateral FTAs it has concluded, which suggests serious difficulties in negotiating a common external tariff. The Region also continues to be characterized by internal political uncertainties (for example, with regard to the future of Kosovo, the future of Serbia and Montenegro, and the workability of the Dayton arrangements in Bosnia and Herzegovina), which would tend to make a customs union difficult to design as well as implement.

Finally, the SEE countries see little value in a customs union with the EU for several political reasons: first, they fear that it may become a substitute for full EU accession, which is their primary and foremost long-term goal; second, they see that they can achieve this long-term goal just as well through an FTA, as many countries in Central and Eastern Europe did, as through a customs union. Indeed, the customs union that Turkey has concluded with the EU, combined with the difficulties the latter has encountered in getting a political commitment

to even starting negotiations for accession, is seen as further proof that a customs union may result in sidetracking the efforts for accession.

On balance, and while there may be some potential theoretical merit in urging the early establishment of a customs union among the SEE countries and between them and the EU, there is more merit to giving high priority to the practical and politically far more acceptable steps to establishing a free trade area among all the SEE countries and to using this area as an eventual springboard for accession to the EU. Once an FTA is agreed on, then individual countries would be well advised to start moving their external tariff toward that of the EU, but each should do so at its own pace. For each country to proceed at its own pace would both ease its future adjustment as well as reduce rents and increase competition and efficiency, but at a pace that would be dictated by its own economic situation.

In the CIS, the economic arguments in favor of a customs union are far weaker. Indeed, there is good reason to believe that a customs union with Russia, on the basis of the Russian tariff, is not in the economic interests of small open economies such as those of the Kyrgyz Republic and Tajikistan or, for that matter, Moldova, which has shown some interest in joining the arrangement. These countries would be better off keeping their existing free trade arrangements with Russia. There is strong evidence that moving to the much higher Russian tariff, which reflects the interests of protected Russian industry, will result in decreases in their welfare as a result of substantial trade diversion and will tend to tie their economies to the old technology of the Russian industrial structures. The only country that can expect welfare gains from a customs union as currently proposed would be Russia.²² On the other hand, if these countries maintain a free trade agreement with Russia (and with each other), they would enjoy the benefits of access to the Russian market without having to incur the high costs of trade diversion that would result from a customs union with Russia that adopts the higher Russian tariff.

Just as it is for the SEE countries, however, the present web of bilateral, partial FTAs with nontransparent rules and arbitrary changes is not the answer. Instead, CIS members should seek to establish a single FTA or perhaps FTAs that cover a few contiguous countries, such as the countries in Central Asia, with comprehensive coverage, clear rules consistently enforced, and an institutional structure that permits review of implementation as well as help in adjudicating disputes.

Regional Integration and WTO Membership

Participation in the Eurasian agreement and regional preferential trade arrangements in general has led to some confusion regarding

the implications of these agreements for WTO membership. A few years back, countries in Central Asia were discussing the two as alternatives: either become a WTO member or join the Eurasian Economic Community. Nothing could be further from the truth. When a country applies for WTO membership, it can be a member of any number of regional preferential arrangements, which however should be compatible with the WTO provisions regarding such arrangements. However, these provisions (Article XXIV of the GATT) are couched in such broad terms that they are typically relatively easy to fulfill. The problem with the preferential arrangements in the Former Soviet Union was a lack of clarity regarding what was covered by the agreements, the rules of origin, exemptions, and so forth.

With regard to the Eurasian Economic Community in particular, its members agreed to apply to join the WTO individually. This means that they recognized the fact that there was no common external tariff in place, as is required by a customs union, but only a free trade area with each of the members having a different tariff structure with regard to imports from the rest of the world. This was clearly understood during the accession negotiations of the Kyrgyz Republic, the first member of the Eurasian agreement to become a member of the WTO. The Kyrgyz Republic accepted legal commitments to bind its tariffs in the WTO at levels significantly lower than the levels applied by Russia, which are supposed to be the levels to be applied by the yet-to-be-formed Eurasian customs union. After the Kyrgyz Republic became a member of the WTO, it notified the WTO of its intention to participate in a customs union with the other countries of the Eurasian agreement (WTO 1999a). Now the Kyrgyz Republic has a problem, however: if it is to join the Eurasian customs union before Russia and the other members of the Eurasian community enter the WTO, it will have to seek a WTO waiver to permit it to raise its tariffs to the level of the Eurasian Community common external tariff. The alternative, and much more desirable, option is for the Kyrgyz Republic to keep its overall tariffs at their present low levels and maintain only an FTA arrangement with its partners in the Eurasian agreement.

At present, Kazakhstan and Belarus are tailoring their bilateral tariff negotiations to those of Russia so that the tariff bindings of the three countries will be at identical levels once they join the WTO. The three countries have stated their desire to enter the WTO as a customs union. It is hard to see how this can happen, given their separate accession processes.

At the same time, the approach has tended to delay Kazakhstan's WTO accession, in addition, as noted earlier, to being of questionable economic value. Given the present status of Kazakhstan's WTO

negotiations, however, it is likely that Kazakhstan will be able to accede to the WTO soon after Russia does. Belarus' WTO accession is problematic, primarily because of the lack of progress on market reform; it has less to do with that country's tariff offers. Ukraine's accession has moved parallel to that of Russia, but the two economies are very different in many respects, as is their tariff structure, so that the notion of a "joint" accession is even more problematic. Thus, the question of whether to form a customs union before or after WTO accession appears to be largely academic. Should some or all of these countries decide to form a customs union after they have become WTO members, then they would have to abide by the WTO rules guiding the formation of customs unions. These include, among other things, the rule that the common external tariff of the customs union not be higher than the weighted average of the countries' individual tariffs.

Conclusions

This analysis of trade policies and institutions of the countries in the Region—primarily in SEE and the CIS—reveals many steps that need to be taken in order to improve these economies' relatively lackluster performance over the last 15 years.

While most of these countries have adopted liberal trade regimes, in a few cases (for example, Uzbekistan), there is still scope for import liberalization so as to eliminate barriers that introduce inefficiencies and hamper growth. Export restraints are present in many of the countries and need to be eliminated in order to ensure effective integration into the world economy. High priority should be given to establishing efficient and prompt rebates of VAT and import duties and eliminating taxes on labor.

Trade-related institutions, and especially customs, inhibit rather than facilitate trade and are in need of major reform; further, domestic regulations and procedures impede rather than facilitate trade. There are major problems in behind-the-border measures that inhibit trade expansion. Services sectors such as banking and finance and transportation, which provide important inputs to trade, are underdeveloped or inefficient. There are important transit issues that inhibit trade for several countries that are both remote and landlocked. There are also important problems of lack of interenterprise competition and weak governance, which adversely affect trade. (All these issues are addressed in the remaining chapters of this study).

By comparison to these domestic restraints to international trade, market access is not a serious general problem affecting these countries' exports. There are, however, problems in particular sectors stemming in part from extensive use of antidumping actions against the countries, as well as developed-country agricultural policies. Some of the market-access problems will be addressed by accession to the WTO. While substantial progress has been made in this area, there are still many countries in the Region that have a long way to go before they can accede. WTO accession is important to improve and secure market access; but it is even more important because it forces countries to strengthen their institutional capacity to trade, as well as introducing stability in the trade regime and locking in trade reforms.

Trade relations with the EU, the major market for many of these countries, are important and have been secured through various types of preferential agreements, which provide especially liberal access to countries of Southeastern Europe. Countries of SEE that have been promised eventual entry to the EU need to undertake major reforms in order to meet the EU requirements. One of the early reforms that would be beneficial for them to undertake is the realignment of their external tariffs to those of the EU.

All of the economies have endeavored to organize regional trade agreements among themselves. The agreements in the SEE appear to involve greater mutual trade liberalization than do those of the CIS. Both, however, are subject to enormous complexity and are focused primarily on the exchange of trade preferences. The main challenges faced by both groups of countries are: (a) how to rationalize the large number of bilateral FTAs into Region-wide agreements; and (b) how to extend regional cooperation beyond preferences in merchandise trade and include such matters as transit facilitation and liberalization of services.

Most of the burden of reform in improving trade performance will unavoidably fall on the countries themselves. The international community, however, has important responsibilities to assist them in a variety of ways. Technical and financial assistance are needed to strengthen national capacity in various trade-related sectors. High priority has been given in this respect to customs reform and related trade-facilitation measures. These efforts need to continue and to expand in more of the countries in the Region.

ANNEX

ANNEX TABLE 3.1

Average MFN Applied Tariffs and Bound Rate by Country in the Region in Recent Years

Reporter	Year	Average MFN applied tariff rate (%)								Binding coverage (%)
		Total goods		Agricultural goods		Industrial goods		Bound rate of all goods		
		Simple avg.	Weighted avg.	Simple avg.	Weighted avg.	Simple avg.	Weighted avg.	Simple avg.	Weighted avg.	
Albania	2001	8.5	8.5	9.9	9.5	8.4	8.2	7.0	7.9	100.0
Armenia	2001	3.3	2.2	8.3	6.6	2.9	1.1	8.5	9.6	100.0
Azerbaijan*	2002	10.1	6.2	13.4	10.3	9.8	5.6	n.a.	n.a.	n.a.
Belarus*	2001	10.6	8.1	9.8	8.7	10.7	8.0	n.a.	n.a.	n.a.
Bosnia & Herzegovina*	2001	5.4	5.1	4.2	6.8	5.4	4.6	n.a.	n.a.	n.a.
Bulgaria	2003	5.4	4.2	16.4	19.0	4.7	3.3	24.2	20.0	100.0
Croatia	2002	6.0	4.7	10.9	11.3	5.6	4.2	5.8	4.8	100.0
Czech Rep.	2003	5.0	4.3	8.2	10.9	4.7	4.0	5.0	4.5	100.0
Estonia	2003	0.2	0.1	2.4	0.9	0.0	0.0	8.6	6.3	100.0
Georgia	2002	10.0	10.6	14.2	15.1	9.5	9.6	7.2	8.3	100.0
Hungary	2002	3.2	2.2	17.4	15.7	2.2	1.7	9.7	8.3	96.2
Kazakhstan*	1996	9.5	n.a.	8.8	n.a.	9.6	n.a.	n.a.	n.a.	n.a.
Kyrgyz Rep.	2001	4.5	3.2	7.1	6.6	4.3	2.7	7.4	6.4	99.9
Latvia	2000	1.2	0.6	5.6	3.4	0.8	0.2	12.7	9.3	100.0
Lithuania	2002	3.5	2.2	8.9	9.4	3.1	1.5	9.2	9.4	100.0
Macedonia, FYR	2001	14.3	11.1	22.5	17.0	13.8	10.2	n.a.	n.a.	n.a.
Moldova	2001	5.1	2.8	11.2	9.2	4.5	2.0	0.0	0.0	100.0
Poland	2003	11.9	11.9	44.3	34.3	9.6	10.6	11.3	8.2	96.3
Romania	1999	24.7	22.8	123.1	126.2	16.3	13.9	40.4	40.3	100.0
Russian Fed.*	2001	10.8	8.9	9.8	8.9	10.9	8.9	n.a.	n.a.	n.a.
Serbia & Montenegro*	2001	9.0	5.8	13.1	11.9	8.7	5.0	n.a.	n.a.	n.a.
Slovak Rep.	2003	4.8	4.6	8.2	14.0	4.6	4.1	5.0	4.7	100.0
Slovenia	2003	11.1	10.0	13.0	14.0	10.9	9.7	23.3	21.3	100.0
Tajikistan*	2002	8.0	7.1	9.8	6.3	7.8	7.3	n.a.	n.a.	n.a.
Turkmenistan*	2002	5.3	2.9	18.9	15.5	3.8	1.1	n.a.	n.a.	n.a.
Ukraine*	2002	7.9	3.9	11.2	15.1	7.8	3.4	n.a.	n.a.	n.a.
Uzbekistan*	2001	10.6	5.9	11.7	3.5	10.6	6.2	n.a.	n.a.	n.a.
Memo:										
European Union (15)	2003	4.4	3.1	6.2	5.2	4.2	3.0	3.9	3.0	100.0

Sources: Based on UNCTAD TRAINS and WTO IDB databases.

Note: Agricultural goods are based on WTO classification of HS 01-24, and industrial goods are HS 25-96.

* Indicates non-WTO member.

Where countries are in bold, all bound tariffs are based on WTO IDB data; others are based on UNCTAD TRAINS data.

ANNEX TABLE 3.2

Antidumping Initiations of Countries in the Region by Product, 1995–2003

Perpetrators	Number of cases	Year of initiation	Target country	Sector	Products
Bulgaria	1	2002	Turkey	Agric	Active baker's yeast
Czech Republic	1	1999	Germany	Manuf	Salt suitable for human consumption (4 products)
	1	1998	Denmark	Agric	Infant milk formula
	1	1998	Netherlands	Agric	Infant milk formula
Latvia	1	2002	Lithuania	Agric	Butter
	1	2002	Lithuania	Agric	Milk
	1	2002	Estonia	Manuf	Portland cement
	1	2002	Hungary	Agric	Honey
	1	2002	Russia	Agric	Honey
	1	2002	Ukraine	Agric	Honey
	1	2001	Belarus (*)	Manuf	Portland cement
Lithuania	1	2000	Belarus (*)	Manuf	Grey portland-cement
	1	2000	Russia	Manuf	Grey portland-cement
	1	2000	Ukraine	Manuf	Grey portland-cement
	1	2000	Latvia (*)	Agric	Nondried baking yeast
	1	2000	Belarus	Manuf	Burnt lime
	1	2000	Russia	Manuf	Burnt lime
	1	1999	Latvia (*)	Manuf	Safety matches
Poland	1	2003	India	Manuf	Graphite electrodes
	1	2002	Czech Rep.	Manuf	Styrene-butadiene rubber (SBR)
	1	2002	Romania	Manuf	Styrene-butadiene rubber (SBR)
	1	2002	Russia	Manuf	Styrene-butadiene rubber (SBR)
	1	1999	China	Manuf	Pocket lighters, gas fuelled, refillable
	1	1999	Taiwan (China)	Manuf	Pocket lighters, gas fuelled, nonrefillable, refillable
	1	1999	Indonesia	Manuf	Pocket lighters, gas fuelled, nonrefillable, refillable
	1	1999	Vietnam	Manuf	Pocket lighters, gas fuelled, nonrefillable, refillable
	1	1999	Belarus	Manuf	Synthetic filament tow of polyesters
	1	1999	Belarus	Manuf	Synthetic staple fibers, not carded, combed
1	1999	Germany (*)	Manuf	X-ray films – type Retina XBM	
1	1997	China	Manuf	Pocket lighters, gas-filled, nonrefillable	
Slovenia	1	1999	Hungary	Agric	Fresh or frozen turkey breast, skinless, boneless
All above (6)	31 cases		18 countries		18 products

Source: Based on semiannual notifications by individual members to the WTO Antidumping Committee.

Note: (*) resulted in price undertakings.

ANNEX TABLE 3.3

Numbers and Share of Antidumping in Countries of the Region by Exporting Economy, 1995–2003

Exporting country	1995	1996	1997	1998	1999	2000	2001	2002	2003	Total
All countries	157	224	243	256	355	294	366	311	210	2,416
Industrial countries ^a	51	69	92	83	88	72	95	68	65	683
Developing countries ^b	86	133	124	129	207	174	231	189	135	1,408
of which: China ^c	20	43	33	28	40	43	53	51	45	356
Countries in the Region ^d										
of which:	20	22	27	44	60	48	40	54	10	325
Belarus	0	0	0	0	3	4	1	1	1	10
Bosnia & Herzegovina	1	0	0	0	0	0	0	0	0	1
Bulgaria	0	3	2	1	1	1	2	0	1	11
Croatia	1	0	0	1	1	1	0	0	0	4
Czech Rep.	1	1	0	2	7	3	2	1	1	18
Estonia	0	0	1	0	0	1	1	1	0	4
Georgia	0	0	0	0	0	0	0	1	0	1
Hungary	2	0	2	2	4	0	3	1	0	14
Kazakhstan	3	1	2	4	0	3	3	6	0	22
Latvia	0	0	2	1	1	3	0	0	0	7
Lithuania	0	0	1	0	4	1	1	3	0	10
Macedonia, FYR	1	0	1	1	1	0	2	1	0	7
Moldova	0	0	0	0	0	2	1	0	0	3
Poland	2	3	3	4	3	5	1	4	0	25
Romania	1	2	1	5	4	4	5	8	2	32
Russian Fed.	2	7	7	12	17	12	9	18	2	86
Serbia & Montenegro	0	0	0	0	0	0	1	0	0	1
Slovak Rep.	0	1	1	1	3	1	2	1	0	10
Slovenia	1	0	0	1	0	0	0	0	0	2
Ukraine	2	3	4	9	9	7	6	8	3	51
Uzbekistan	2	0	0	0	0	0	0	0	0	2
Yugoslavia	1	1	0	0	2	0	0	0	0	4
Share of total (%):										
Industrial countries	32.5	30.8	37.9	32.4	24.8	24.5	26.0	21.9	31.0	28.3
Developing countries	54.8	59.4	51.0	50.4	58.3	59.2	63.1	60.8	64.3	58.3
of which: China	12.7	19.2	13.6	10.9	11.3	14.6	14.5	16.4	21.4	14.7
Region's countries	12.7	9.8	11.1	17.2	16.9	16.3	10.9	17.4	4.8	13.5

Source: WTO Antidumping Committee.

Note:

- a. Includes Australia, Canada, 15 European Union members, Iceland, Japan, New Zealand, Norway, Switzerland, and the United States.
b. Includes all other countries and China, excluding industrial and transition countries.
c. Excludes Hong Kong (China), Macao, and Taiwan (China).
d. Includes 27 transition countries in the Region, excluding Turkey with 34 initiations.

ANNEX TABLE 3.4

Trade Coverage of SEE FTAs in the Agricultural and Manufacturing Sectors

FTA 1	Country 2	Share of harmonized system (HS) tariff lines freed (%)			Share of bilateral imports liberalized (%)			Criteria t = tariff line i = import- based	
		All products 3	Agriculture 4	Manufacturing 5	All products 6	Agriculture 7	Manufacturing 8		
GROUP III									
24.	MAC-ROM	Macedonia, FYR	84.9	0.3	98.6	86.0	0.0	100.0	
23.	MAC-MOL	Macedonia, FYR	85.0	0.3	98.8	19.5	0.0	100.0	
15.	BUL-MAC	Macedonia, FYR	86.3	0.3	100.0	87.2	0.0	100.0	t<88%
24.	MAC-ROM	Romania	86.3	10.3	98.6	59.8	0.0	100.0	i<88%
6.	ALB-ROM	Romania	86.5	10.3	98.9	82.0	0.0	100.0	
2.	ALB-BUL	Bulgaria	87.0	11.0	99.4	83.8	0.0	100.0	
3.	ALB-CRO	Croatia	87.4	14.2	99.0	53.2	0.0	100.0	
20.	CRO-MOL	Croatia	87.4	14.5	99.2	81.0	0.0	100.0	
21.	CRO-ROM	Romania	87.6	11.2	99.8	71.4	0.5	100.0	
23.	MAC-MOL	Moldova	87.3	13.7	99.2	97.9	0.0	100.0	
20.	CRO-MOL	Moldova	87.4	15.0	99.2	100.0	—	100.0	t<88%
18.	BUL-S&M	Serbia & Montenegro	87.6	15.0	99.4	94.0	2.5	99.9	i>88%
15.	BUL-MAC	Bulgaria	87.7	10.9	100.0	89.1	0.8	100.0	
GROUP II									
21.	CRO-ROM	Croatia	88.1	14.2	99.9	47.8	0.4	100.0	
18.	BUL-S&M	Bulgaria	88.4	19.3	99.6	87.4	45.1	99.7	t>88%
16.	BUL-MOL	Bulgaria	88.7	22.8	99.4	43.9	29.1	100.0	i<88%
2.	ALB-BUL	Albania	88.9	23.7	99.5	75.5	18.3	100.0	
16.	BUL-MOL	Moldova	89.9	30.7	99.5	84.0	11.9	100.0	
3.	ALB-CRO	Albania	88.2	23.3	98.6	95.8	0.0	100.0	
6.	ALB-ROM	Albania	88.4	23.7	99.0	99.6	80.4	100.0	
28.	ROM-S&M	Serbia & Montenegro	88.5	20.3	99.5	96.9	1.0	99.9	t>88%
12.	BIH-ROM	Romania	88.7	28.4	98.5	89.9	0.0	100.0	i>88%
28.	ROM-S&M	Romania	88.8	22.4	99.6	89.9	3.4	100.0	
8.	BIH-BUL	Bulgaria	88.9	24.6	99.3	95.6	0.0	97.6	
7.	ALB-S&M	Serbia & Montenegro	89.3	27.0	99.4	99.6	31.1	100.0	
8.	BIH-BUL	Bosnia & Herzegovina	91.5	42.0	99.5	75.9	7.9	97.1	
12.	BIH-ROM	Bosnia & Herzegovina	91.8	43.3	99.6	83.7	61.3	100.0	
7.	ALB-S&M	Albania	92.0	45.8	99.5	39.1	16.8	100.0	t>90%
5.	ALB-MOL	Albania	92.5	49.2	99.5	36.4	0.0	100.0	i<88%
4.	ALB-MAC	Albania	93.8	57.8	99.5	79.9	20.9	99.9	
22.	CRO-S&M	Serbia & Montenegro	94.2	61.9	99.4	80.0	23.1	99.9	
19.	CRO-MAC	Croatia	99.1	93.3	100.0	87.8	26.6	100.0	

(Table continues on the following page.)

ANNEX TABLE 3.4 (continued)

FTA 1	Country 2	Share of harmonized system (HS) tariff lines freed,(%)			Share of bilateral imports liberalized (%)			Criteria t = tariff line i = import- based	
		All products 3	Agriculture 4	Manufacturing 5	All products 6	Agriculture 7	Manufacturing 8		
GROUP I									
1.	ALB-BIH	Bosnia & Herzegovina	93.0	51.4	99.7	88.6	0.0	100.0	t>90%
4.	ALB-MAC	Macedonia, FYR	93.1	52.0	99.6	89.6	65.0	100.0	i>88%
19.	CRO-MAC	Macedonia, FYR	99.3	94.9	100.0	88.8	58.7	100.0	
5.	ALB-MOL	Moldova	91.7	43.9	99.4	100.0	—	100.0	
1.	ALB-BIH	Albania	92.6	49.9	99.6	91.7	59.5	100.0	
14.	BUL-CRO	Bulgaria	93.9	59.8	99.3	95.6	17.8	100.0	
14.	BUL-CRO	Croatia	94.5	62.1	99.7	91.7	79.1	100.0	
17.	BUL-ROM	Romania	94.6	62.1	99.8	94.4	58.6	100.0	
17.	BUL-ROM	Bulgaria	94.6	61.5	100.0	98.0	48.1	100.0	
22.	CRO-S&M	Croatia	94.7	62.1	100.0	90.3	54.3	100.0	
27.	MOL-S&M	Moldova	99.5	96.6	100.0	97.4	24.9	100.0	t>90%
27.	MOL-S&M	Serbia & Montenegro	99.5	96.6	100.0	99.2	99.0	100.0	i>90%
25.	MAC-S&M	Macedonia, FYR	100.0	100.0	100.0	99.9	100.0	99.8	
25.	MAC-S&M	Serbia & Montenegro	100.0	100.0	100.0	99.9	100.0	99.9	
10.	BIH-MAC	Bosnia & Herzegovina	100.0	100.0	100.0	100.0	100.0	100.0	
10.	BIH-MAC	Macedonia	100.0	100.0	100.0	100.0	100.0	100.0	
11.	BIH-MOL	Bosnia & Herzegovina	100.0	100.0	100.0	100.0	100.0	100.0	
11.	BIH-MOL	Moldova	100.0	100.0	100.0	100.0	-	100.0	
13.	BIH-S&M	Bosnia & Herzegovina	100.0	100.0	100.0	100.0	100.0	100.0	
13.	BIH-S&M	Serbia & Montenegro	100.0	100.0	100.0	100.0	100.0	100.0	
26.	MOL-ROM	Moldova	100.0	100.0	100.0	100.0	100.0	100.0	
26.	MOL-ROM	Romania	100.0	100.0	100.0	100.0	100.0	100.0	
9.	BIH-CRO	Bosnia & Herzegovina	100.0	100.0	100.0	100.0	100.0	100.0	
9.	BIH-CRO	Croatia	100.0	100.0	100.0	100.0	100.0	100.0	

Source: National statistics, bilateral imports 2002 (2001 for Serbia and Montenegro). Imports for Bosnia and Herzegovina are replaced by partner country's exports. Agriculture: Harmonized System (HS) chapters 1 to 24; Manufacturing: HS chapters 25 to 97.

Endnotes

1. For a summary review of the same issues five years ago, at the end of a decade of transition, see Michalopoulos (2001); for a similar review of Russia and Ukraine, see Michalopoulos (1999).
2. The discussion in this section focuses primarily on trade policies in the transition economies that are not members of the EU.
3. There is little information such as, for example, a tariff schedule on formal trade restrictions in Turkmenistan. There is a general impression that the flow of imports is controlled through licensing and other NTBs.
4. This, however, does not mean that the agricultural sector as a whole receives more support than industry. Border protection is only one of several elements in calculating aggregate measures of support (AMS) to the sector.
5. For example, agricultural tariffs in Ukraine average 30 percent if specific rates are taken into account, not 15 percent, as shown in annex table 3.1; some rates even exceed 100 percent.
6. Albania, Armenia, Bulgaria, Croatia, Georgia, the Kyrgyz Republic, FYR Macedonia, Moldova, and Romania.
7. "Bound" tariff levels are maximum levels of tariffs that WTO members have committed to maintain.
8. These standards pertain to the freedom of access to foreign exchange for transactions in the current account of the balance of payments.
9. These are 39 percent in the Kyrgyz Republic—although there were proposals for their reduction.
10. In what follows, we summarize the findings from various studies undertaken by the governments or donors. As the problems in Tajikistan and Uzbekistan have not been extensively studied, there are far fewer references to these countries. This should not be interpreted to mean that they face fewer problems.
11. It is unclear whether this practice has been continued post-WTO accession in Armenia.
12. This is not always their fault, as some foreign governments change requirements frequently and without notice. A Georgian wine exporter reported that Russia recently changed labeling standards three times in a 12-month period (World Bank 2003d).
13. Serbia and Montenegro have recently announced that they will pursue WTO accession separately.
14. The totals include transition economies who are currently members of the EU.
15. There is no evidence that export subsidies by the transition countries are the reason for the frequency of antidumping measures against them. In any case, if there were export subsidization, the proper remedy would be countervailing tariffs, not antidumping.
16. The MOU was negotiated and signed by Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, Romania, and the Federal Republic of Yugoslavia (as of 2003, Serbia and Montenegro). Moldova signed on to the MOU although it did not participate in its negotiation. In 2004 the United Nations Mission in Kosovo (UNMIK), on behalf of

Kosovo, formally declared its intention to abide by the MOU provisions and sign FTAs with countries in the Region.

17. As the Council Regulation (No. 2007/2000), September 2000, stated, "the entitlement to benefit from the preferential arrangement shall equally be subject to their readiness to engage in regional cooperation with other countries concerned by the European Union's Stabilization and Association process, in particular through the establishment of free trade areas in conformity with Article XXIV of the GATT 1994 and other relevant WTO provisions." This provision has also mitigated the "Hub and Spokes" problem that sometimes tends to characterize preferential trade arrangements between developed and developing countries (Kaminski and de la Rocha 2003a).
18. See Messerlin and Miroudot (2004).
19. Collaboration among the countries in a variety of trade-related facilitation measures has been assisted by many donors, including the World Bank-led TTFSE (Trade and Transport Facilitation in South Eastern Europe) multicountry project. Nevertheless, recent surveys suggest that many problems continue to persist (European Commission 2004).
20. Moldova was given observer status in the agreement in 2002.
21. Russia dominates the council, which provides operational direction to the agreement: it has four votes, compared to two each for Kazakhstan and Belarus and one each for the Kyrgyz Republic and Tajikistan.
22. For a detailed discussion, see Tumbarello (2004); Michalopoulos and Tarr (1997); and Olcott, Ashlund, and Garnett (1999).