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Tajikistan Joining the Customs Union of Russia, Belarus and Kazakhstan: Pros and Cons

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In this brief we summarize the results obtained in a CEFIR research project on the economic impact of Tajikistan joining the Customs Union of Russia, Belarus and Kazakhstan conducted for the Eurasian Development Bank in 2013 (EBD, 2013). We argue that integration has to be comprehensive to be mutually beneficial: indeed, trade effects are marginal, and the highest stakes are at migration regulation in the CU member-countries and the investment opportunities in Tajikistan.

The creation of the Customs Union (CU) between Russia, Belarus and Kazakhstan (RuBeKa) suggested a possible format of a supranational organization in the ex-Soviet Union space. The core of the Customs Union is cemented with the political will of the leaders of the three countries, which is aimed on further integration and calls for the removal of all barriers to the Common Economic Space by January 1, 2015. In turn, the Common Economic Space of Russia, Belarus and Kazakhstan imply freedom of movement of goods, services, and financial and human capital across the borders of the participating countries.

The logic of integration process advocates for an enlargement of the RuBeKa CU. From an economic viewpoint, enlargement may seem as a very ambitious intention: forces of economic gravity dictate that RuBeKa (with 3% of the world GDP in 2011) could find it very difficult to overcome the influence of the EU (17%) on RuBeKa’s Western boarder and that of China (10%) on its Eastern boarders. Nevertheless, there is a vivid discussion about enlargement, with one of regions in focus being Central Asia. Two countries of this region, Kyrgyzstan and Tajikistan, are sending mixed signals about their willingness to enter RuBeKa. In this brief we summarize the results obtained in a CEFIR research project on the economic impact of Tajikistan joining the Customs Union of Russia, Belarus and Kazakhstan conducted for the Eurasian Development Bank in 2013 (EBD, 2013).

Background: Tajikistan

Tajikistan is one the poorest countries of Central Asia, with its nominal GDP per capita equal to $872 in 2012 (WB WDI). It is a highland, landlocked country almost ruined by a devastating 5-year civil war that broke out soon after the declaration of independence in 1992. Nowadays, the core of the Tajik economy consists of cultivation of cotton, textile and lighter industries, power generation, aluminum production, extraction of natural resources (gold, silver, antimony...
and coal), as well as production of some consumer goods.

The low base effect could partly explain recent high growth rates of Tajikistan: real GDP growth rate was 7.4% in 2011, with real GDP per capita growth rate being equal to 5.9%. The main drivers of Tajikistan’s GDP growth are remittances from massive labor migration to neighboring countries (mainly Russia) and export growth (with main export commodities being aluminum and cotton).

**Figure 1. Structure of Exports of Tajikistan in 2011**

![Structure of Exports of Tajikistan in 2011](image)

*Source: Agency on Statistics under President of the Republic of Tajikistan*

**Tajikistan and RuBeKa**

An enlargement of RuBeKa to Tajikistan could have a profound effect on the Tajik economy, since Russia, Belarus and Kazakhstan are currently discussing a package of trade, migration and investment policy measures.

**Trade**

On the trade side, there is not much to catch: most of the tariffs on bilateral trade between Russia, Belarus and Kazakhstan with Tajikistan are zero due to the Eurasian Economic Community treaties. The external tariff of the CU is somewhat higher than the current in Tajikistan: average weighted external tariff of the CU is 7.55% versus 6.41% in Tajikistan, as of the end of 2013.

**Table 1. Simple average and weighted ad valorem tariffs for the Customs Union and the Republic of Tajikistan for the end of 2013 and for 2020 for sectors of GLOBE model, %**

<table>
<thead>
<tr>
<th>Sector</th>
<th>End of 2013, %</th>
<th>Year 2020, %</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Average</td>
<td>Weighted</td>
</tr>
<tr>
<td>Agricultural products</td>
<td>4.9</td>
<td>4.3</td>
</tr>
<tr>
<td>Coal</td>
<td>6.0</td>
<td>6.4</td>
</tr>
<tr>
<td>Oil</td>
<td>1.4</td>
<td>1.4</td>
</tr>
<tr>
<td>Gas</td>
<td>2.5</td>
<td>2.5</td>
</tr>
<tr>
<td>Other mining</td>
<td>6.0</td>
<td>6.0</td>
</tr>
<tr>
<td>Food</td>
<td>13.6</td>
<td>13.6</td>
</tr>
<tr>
<td>Textiles</td>
<td>10.5</td>
<td>10.5</td>
</tr>
<tr>
<td>Other manufacturing</td>
<td>4.7</td>
<td>4.7</td>
</tr>
<tr>
<td>Chemicals</td>
<td>7.9</td>
<td>7.9</td>
</tr>
<tr>
<td>Other minerals</td>
<td>12.5</td>
<td>12.5</td>
</tr>
<tr>
<td>Metals</td>
<td>8.5</td>
<td>8.5</td>
</tr>
<tr>
<td>Electricity</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Manufacture of goods, etc.</td>
<td>1.0</td>
<td>1.0</td>
</tr>
</tbody>
</table>

*Source: CEFIR calculations*

Tajikistan is a member of WTO since March 2013, which means that any regional trade agreement should obey Article XXIV stating “a regional trade agreement should aim to boost trade between its member countries and not to raise barriers against the trade with other WTO members” (WTO, 2005). Taking into account the WTO regulations, an enlargement
of the RuBeKA should not increase Tajikistan’s trade barriers, thus leaving questions on how the external tariff on a new enlarged CU could be formed.

The magnitude of the possible effects of Tajikistan joining RuBeKa could be assessed using the computable general equilibrium model GLOBE (McDonald et al., 2007). With the assumption that Tajikistan would use RuBeKa’s external tariff, the change in GDP induced by enlargement equals 0.2% for Tajikistan, 0.1% for Russia, and is negative for Belarus and Kazakhstan (-0.05% and -0.003%, accordingly). In case Tajikistan is to join the CU, the net GDP loss of Belarus and Kazakhstan need a special settlement procedure, involving transfers from Russia to its partners.

One trade aspect that is not incorporated into the CGE model is a dynamic change in the composition of exports due to realizations of export potential in the sense of the Hausmann and Klinger approach (Hausmann & Klinger, 2006, 2007). This approach focuses on the relationship between the current export structure of a country and its future development. Hausmann and Klinger use “complexity” of the export basket as a proxy for the structure of this basket. The level of “complexity” is determined by the level of development in countries that have a similar structure of exports. Assessing the dynamics of this complexity, Hausmann and Klinger propose a methodology to predict the development of the current exports of the country. This methodology is based on the assumption that the evolution in the bundle of goods, constituting the revealed comparative advantage of the country in question, is to a large extent determined by the “closeness” of these goods to the current basket of exports.

Presently, Tajik exports definitely lack “complexity”, but it is possible to increase it. According to EDB (2013) findings, trade with the countries of the Customs Union allows Tajikistan to increase the “complexity” of its exports more, than it would without integration.

All manufactured goods can be divided into four large groups (Lall, 2000): “resource based manufactures”, “low technology manufactures”, “medium technology manufactures”, and “high technology manufactures”. The results of the Hausmann model applied to Tajikistan show that Tajikistan now can increase the production of the following goods, which have the highest export potential:

- Medium-technology goods: refrigeration equipment;
- Low-technology goods:
  - construction materials made of stone, cement and wood;
  - aluminum products;
  - textile and apparel;
  - milk diary products;
  - fish products.

**Labor Migration**

According to EDB (2012), labor migration from Tajikistan to Russia started to grow in 2005 from a modest 40,000 people to an impressive 400,000 registered labor migrants in 2008. However, this is only the visible part of the iceberg. In 2010, there were 268,000 registered labor migrants from Tajikistan in Russia and up to 650,000 illegal migrants working in Russia (EDB, 2012).

In the case of deep integration with Russia, Belarus and Kazakhstan, EDB (2011) suggests that a significant portion of Tajik illegal workers would legalize their status. This could increase the Russian budget revenue; according to EDB (2011), the Russian budget loses between 10 and 40 billion rubles per year in personal income tax alone since illegal migrant workers do not pay taxes.

The labor migration part of the deal consists of several agreements aimed to remove barriers for labor migration from Tajikistan, and
provide social security for labor migrants and their families. Legislative measures aimed to legalize Tajik labor migrants could increase their effective wages by 9 to 28%. With the assumption of steady demand for labor migrants from CU countries, labor migration from Tajikistan could then increase by 10 to 15%, which could generate 15 to 25% higher remittances for Tajikistan. As remittances are one of the main drivers of the Tajik economy, this perspective could be very appealing for the Tajik government.

**Investments**

The remittance flow is not channeled to investment due to the low confidence in the banking sector. Tajikistan has a very low level of private investment - only 5% of GDP (World Bank, 2011). According to ILO (2010), households save up to 23% of remittances, which corresponded to almost 300 million USD in 2008. However, they do not use banks for these savings.

The World Bank (World Bank, 2011) states that remittances will be an important factor for future growth, but it is necessary to increase investments. Also, the fact that Tajikistan depends on remittances is a significant source of macroeconomic vulnerability. The efficient use of remittances can increase investments and capital stock, which would allow the Tajik economy to increase real GDP growth rate by one percentage point (EDB, 2013).

The investment potential of Tajikistan is high. Main sectors for investment are non-ferrous metals, hydropower, as well as food and lighter industries (mostly textile). Tajikistan could be an interesting investment opportunity for the CU’s companies, but the World Bank’s BEEPS survey conducted in 2009 recorded many obstacles to business activities, such as a bad investment climate, high taxation, blackouts, corruption, customs administration and trade regulation (EDB, 2013). Improvement of the investment climate is therefore a key component for a success story, and would help realizing the benefits of Tajikistan integrating with Russia, Belarus and Kazakhstan.

**Conclusion and Policy Implications**

Summing up, our analysis of the possible effects of Tajikistan joining the Customs Union of Russia, Belarus and Kazakhstan suggests that the main economic benefits for Tajikistan lie in the supplement agreements, mainly in the labor migration sphere. Tajikistan’s economic benefits of trade integration are quite modest, revealing that the driving force of this integration process lies in the political domain.

- The above findings also raise a number of policy-relevant points: Integration have to be comprehensive to be mutually beneficial; trade effects are marginal; and the highest stakes of integration regards migration regulation in the CU member-countries and investment opportunities in Tajikistan.
- Migration regulation is one of the cornerstones of a possible integration: Russian interest regards legalizing migration flows and Tajik interest is in stabilizing flow of remittances.
- It is crucial for Tajikistan to increase the confidence in the banking system, which is possible with the help of investments from the other CU members.
- An improvement of the investment climate is the key component of a success story, which will help realizing the benefits of a Tajik integration with Russia, Belarus and Kazakhstan.
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