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Non-Tariff Barriers and Trade Integration in the EAEU

It is a commonly held view that the Eurasian Economic Union (EAEU) is a political enterprise (Popescu, 2014) that has little economic meaning other than redistribution of oil rents (Knobel, 2015). With a new reality of low oil prices and reduced rents, a legitimate question is how stable this Union is, or whether there is any hope for mutual economic benefits that can provide incentives to all the participants to maintain their membership in the Union? Our answer is yes, there is hope, but only if countries, especially Russia, make progress on deep integration such as services liberalization, trade facilitation, free movement of labor and especially in the reduction of the substantial non-tariff barriers (NTBs). NTBs are hampering trade both within the Union (World Bank, 2012; Vinokurov, 2015), as well as against third country imports. Our research shows (see Knobel et al., 2016) that all the EAEU members will reap benefits from a reduction of NTBs against each other, but they will obtain considerably more substantial gains from a reduction in NTBs against imports from the EU and China.



Since the early stages of creation of the Customs Union (CU) between Belarus, Kazakhstan, and Russia back in 2010, the economic benefits of the CU have been questionable. The main reason for this in Kazakhstan was the increase in its import tariffs in order to implement the common external tariff of the CU, which initially was Russia's external tariff (Tarr, 2015). Kazakhstan almost doubled its average tariff from 5.3% to 9.5% (Shepoltylo, 2011; Jondosov and Sabyrova, 2011) in the first year of its CU accession. Belarus did not increase its average tariff, but the structure of its tariffs shifted toward a protection of Russian industry.

In 2015, the CU was transformed into the EAEU, and Armenia and Kyrgyz Republic have joined the EAEU. These two countries are WTO members; Kyrgyzstan entered the WTO in 1998, and Armenia in 2001. In 2014, the simple average most-favored nation (MFN) applied tariff rate in Armenia was 3.7%, and 4.6% in the Kyrgyz Republic. Due to differences between Armenia and Kyrgyzstan's WTO commitments and the EAEU tariff schedule, the new members of the EAEU are not implementing the full EAEU tariff schedule. That is, they have numerous exemptions. However, they have started a WTO commitments modification procedure.

Despite adverse impacts from the higher import prices from implementing the common external tariff of the EAEU in Armenia and the Kyrgyz Republic, there are potentially offsetting gains. Given the importance of remittances to the Kyrgyz Republic, the benefits coming from the right of workers to freely move and legally work inside EAEU likely dominate the tariff issues. Armenia also benefits from the free movement of labor, receives Russian gas free of export duties, and wants to preserve the military guarantee granted by Russia through the six-country Collective Security Treaty Organization.

In the case of Belarus, it receives Russian oil and natural gas free of export-duties, which, when oil prices were high, tended to dominate their calculus. Kazakhstan hopes for more FDI as a

platform for selling to the EAEU market; but President Nazarbaev has expressed concerns that the EAEU is not providing net benefits to his country.

To date, the members have judged participation to be in their interest, but with the plunge in the price of oil and gas, the calculus could swing against participation in the EAEU. That is why it is so important to achieve progress with deep integration in the EAEU. One of the most important areas of deep integration for the EAEU is the substantial reduction of non-tariff barriers in goods trade, both between the EAEU members and against third countries. Estimates by the Eurasian Development Bank (Vinokurov et al., 2015) reveal that NTBs account are 15% of the value of intra-union trade flows.

In our paper, Knobel et al (2016), we estimate substantial gains to all the EAEU members from a reduction of NTBs. We employ a global computable general equilibrium model with monopolistic competition in the Helpman-Krugman style based on Balisteri, Yonezawa, Tarr (2014). Estimates of the ad-valorem equivalents of NTBs were based on Vinokurov et al (2015) for the EAEU member countries and Kee, Nicita, Olarreaga (2009) for non-members.

We find that the effects of deep integration are positive for all countries of the EAEU. Armenia's accession to the EAEU will have a strong positive effect only if coupled with a decrease of non-tariff barriers. Armenian accession is associated with an increase in external tariffs, which causes a negative economic impact and decrease in output.

The effect of deep integration in the EAEU will be even greater if any spillovers effect reducing NTBs for EAEU's major trading partners are present. Knobel et al. (2016) simulate a 50% decrease in "technical" NTBs inside the EAEU and a 20% spillover effect of reduction NTBs toward either the EU and USA or China. Reduction of NTBs in trade with the EU and the USA dominates the comparable reduction of NTBs with China for all countries of the EAEU in terms of the welfare gain. Armenia's welfare



gain with a spillover effect towards the EU is 1.1% of real consumption compared to 1.02% with a spillover effect towards China. Growth in welfare in Belarus will be 2.7% with a EU spillover versus 2.5% with a spillover effect towards China. Kazakhstan's gain in real consumption is also greater in the first (EU+USA) case: 0.86% versus 0.66% (with spillover towards China). Russia's gain in real consumption in the case of a spillover effect with the EU is 2.01% versus 0.63% in the case of China.

Summing up, our findings suggest an answer to the recent concern about stability of the EAEU. We think that eliminating NTB, hampering mutual trade, and decreasing NTBs in either European or Chinese direction could provide mutual economic benefits that could tie countries of the EAEU together, thereby giving a much needed solid economic ground for the Union.

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