

Identification of New Market Opportunities within Eurasian Economic Union (EEU)



OSCE Organization for Security and
Co-operation in Europe
Office in Yerevan



**MINISTRY OF ECONOMY
OF THE REPUBLIC OF ARMENIA**

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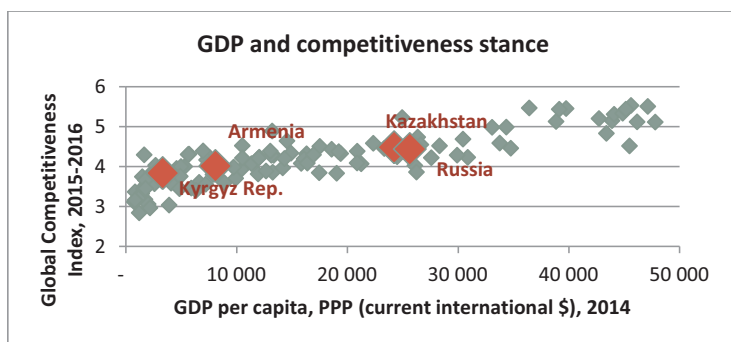
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CHAPTER 1. WHAT IT IS LIKE WITHIN EEU: KEY MACROECONOMIC TRENDS

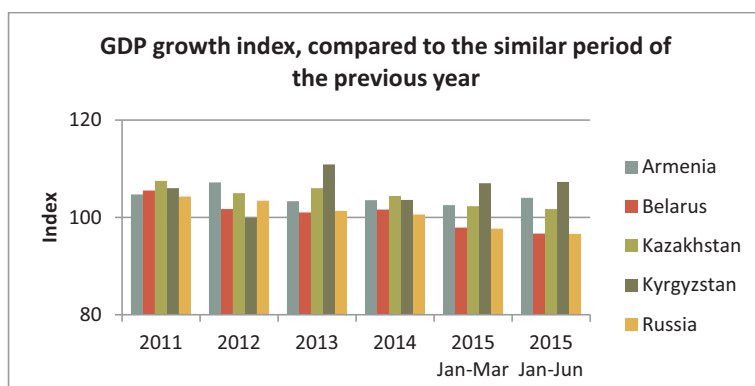
Armenia's entry into Eurasian Economic Union (EEU) started a huge wave of discussions over the advantages and disadvantages of Armenia in pursuing the path of integration. Political, social and economic challenges were the main topics of debates. The rapidly worsening economic situation in EEU countries in the beginning of 2015 intensified the negative outlooks for Armenia, too. The prevailing expectations are about possible deterioration in the local economy due to the high exposure to economies in recession. Armenia's vulnerability to external shocks and developments in Russia in particular is reasoned by the local economy's strong dependence on private transfers from Russia. The volume of the remittances is calculated to sum up to 40% of GDP, including both officially recorded and unrecorded flows. Clearly, the local economy is very sensitive to even slight changes in the flows. According to the Central Bank of Armenia the volume of private remittances transferred via banks in 2014 reduced by 7.7%, from USD 2.3bln in 2013 to USD 2.1bln in 2014. Russia accounts for over 70% of the transfers. The declining trend continued in 2015, the total remittances sent to Armenia in 2015 dropped by 30 per cent compared to 2014 and reached 1.2 bln. USD.

The concerns regarding the future of Armenia are reasoned both by the current weak competitiveness stance of the Union's member countries and by the dynamics of economic development. Both by income per capita and competitiveness indices EEU countries are ranked worse than over 40 countries in the world. This means that there is no highly competitive economy in the Union which can share its practices and set standards for the other members of the Union.



Sources: World Development Indicators, the WB; World Economic Forum

The second, more important issue is the recent trends in the economic development of EEU countries. Two of the most significant countries in the Union – Russia and Belarus, stand out with negative GDP performances in 2015. As a small open economy and part of an economic union, Armenia's development prospects are now even more vulnerable externally and dependent on the situation of EEU member states. The recorded GDP decrease in Russia and Belarus in the first quarter of 2015 not only continued but also demonstrated higher decrease rate in the second quarter.



Sources: The Interstate Statistical Committee of the CIS, National Statistical Offices

Other macroeconomic indicators showed similar negative trends, as well.

Key macroeconomic indicators in EEU countries, 2015 Jan-Jun, compared to the similar period of 2014, index

	Gross domestic product	Industrial production	Agricultural production	Capital investment in fixed capital	Cargo transportation	Retail trade
Armenia	105.1	105.1	114.5	100.6	106.5	93.5
Belarus	96.7	92.6	102.7	86.5	99.3	101.1
Kazakhstan	101.7	100.6	103	104.4	102.4	102.9
Kyrgyz Rep	107.3	123.6	102.4	106.8	102.4	105
Russia	96.6	97.3	102.9	94.6	91.9	92

Sources: The Interstate Statistical Committee of the CIS, National Statistical Offices

The disturbing performance and gloomy forecasts of growth were immediately reflected in the credit ratings of the countries. Moody's, which downgraded its ratings at the beginning of the year, holds negative outlooks for Armenia, Belarus and Russia. Fitch still has stable outlooks for Kazakhstan and Armenia, but Russia's credit profile is assessed as highly risky with negative outlooks by all agencies.

Credit ratings of EEU countries

	S&P rating		Moody's rating		Fitch rating	
Armenia			Ba3	negative	B+	stable
Belarus	B-	stable	Caa1	negative		
Kazakhstan	BBB	negative	Baa2	stable	BBB+	stable
Kyrgyz Republic						
Russia	BB+	negative	Ba1	negative	BBB-	negative

Sources: Trading Economies

In its recent publication of "World Economic Outlook, October 2015" International Monetary Fund reviewed its predictions on GDP growth. The intensifying recession in Russia was assessed to sum up at 3.8% decline at the end of 2015. This is mainly reasoned by the fall in the global oil prices. The downturn

is expected to be accompanied by high inflation rates in Russia - 15.8% in 2015. Meanwhile, Armenia's previously forecasted decrease (-1%, WEO, April 2015) was upgraded to positive 2.5% change.

IMF forecasts on GDP annual growth rate, %

IMF	2015	2016	Reference
Armenia	2.5	2.2	Oct-15
Belarus	-2.3	-0.1	Apr-15
Kazakhstan	2	3.2	Apr-15
Kyrgyz Republic	1.7	3.4	Apr-15
Russia	-3.8	-0.6	Oct-15

Sources: Trading Economies

Despite the difficult 2015, the prospects for 2016 are not too bad. Russia and Belarus are expected to record an insignificant decline in economic activities, whereas Armenia, Kazakhstan and Kyrgyz Republic will probably demonstrate steady growth.

CHAPTER 2. THE IMPACT OF THE SINGLE CUSTOMS UNION ON INTERNATIONAL TRADE

2.1. Foreign trade trends in Armenia by country groups

The analysis of the country trade structure for Armenia with the EEU countries shows that Armenia's main and largest trade partner within the EEU was and remains the Russian Federation, with around 95% of all Armenia's trade with the EEU countries falling on Russia. Armenia has grown its export to Russia on a year-by-year basis, and so have been the imports from Russia, with an overall trade balancing around USD 1.4-1.5 bln a year. In country scale, there is almost no trade between Armenia and Kazakhstan, with annual trade turnover being less than USD 10 mln for the last three years. At the same time, there is a structural change in the trade between Armenia and Kazakhstan: in the years 2010-2012 the trade was exceeding USD 10mln annually and the bulk of trade was Armenia's import from Kazakhstan, whereas in the years of 2013-2014 and the first months of 2015 there is more export to Kazakhstan and almost no import from Kazakhstan (less than USD 1 mln a year). With Belarus the trade volume is more stable, with an annual turnover being in between USD 30-40mln for the last 5 years.

2010: Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)

Source: National Statistical Service of the Republic of Armenia

Year	2010 EEU	% of total	of which	Russia	% of total	Kazakhstan	% of total	Belarus	% of total
Export	168171.8	16.1		160507.8	15.4	3083.3	0.3	4580.7	0.4
Import	879075.4	23.4		835271.7	22.7	11894.4	0.3	31909.3	0.8
Total	1047247.2	21.8		995779.5	20.7	14977.7	0.3	36490	0.8

2011: Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)

Source: National Statistical Service of the Republic of Armenia

Year	2011 EEU	% of total	of which	Russia	% of total	Kazakhstan	% of total	Belarus	% of total
Export	232622.5	17.4		222273.7	16.6	4398.5	0.33	5950.3	0.4
Import	945783.6	22.8		890873.2	21.4	25335.9	0.61	29574.5	0.7
Total	1708406.1	31.1		1113146.9	20.3	29734.4	0.54	35524.8	0.6

2012: Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)

Source: National Statistical Service of the Republic of Armenia

Year	2012 EEU	% of total	of which	Russia	% of total	Kazakhstan	% of total	Belarus	% of total
Export	289783.4	21		279109.0	20.2	3964.1	0.3	6710.3	0.5
Import	1099901.7	25.8		1057416.4	24.8	8896.5	0.2	33588.8	0.8
Total	1389685.1	24.6		1336525.4	23.6	12860.6	0.2	40299.1	0.7

2013: Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)

Source: National Statistical Service of the Republic of Armenia

Year	2013 EEU	% of total	of which	Russia	% of total	Kazakhstan	% of total	Belarus	% of total
Export	349980.6	23.6		334125.7	22.5	7293.3	0.48	8561.6	0.6
Import	1066774.8	24.3		1025159.7	23.3	740.3	0.01	40874.8	0.9
Total	1416755.4	24.1		1359285.4	23.1	8033.6	0.01	49436.4	0.8

2014: Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)

Source: National Statistical Service of the Republic of Armenia

Year	2014 EEU	% of total	of which	Russia	% of total	Kazakhstan	% of total	Belarus	% of total
Export	324238.5	20.9		308250.2	19.9	6951.8	0.4	9036.5	0.6
Import	1154463.8	26		1122876.0	25.3	556.3	0.01	31031.5	0.7
Total	1478702.3	24.7		1431126.2	23.9	7508.1	0.1	40068.0	0.7

2015: Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)

Source: National Statistical Service of the Republic of Armenia

Year	2015 EEU	% of total	of which	Russia	% of total	Kazakhstan	% of total	Belarus	% of total
Export	236246.5	15.9		225927.2	15.1	4857.7	0.3	5461.8	0.4
Import	982124.6	30.1		948044.6	39.1	292.4	0.009	33787.6	1.04
Total	1218371.1	25.7		1173971.8	24.8	5150.1	0.1	39249.4	0.8

Armenia's Trade with the Countries of the European Union in 2010-2015

The analysis of trade between Armenia and the EU shows a constant growth in trade volumes, with trade reaching almost USD 1bln in 2014. The growth is recorded both in terms of Armenian exports to the EU and Armenian imports from the EU. However, one can see that while Armenia's export to the EU was rather stable and the growth was not sharp with up and downs through the last 5 years, whereas Armenia's imports from the EU grew steadily by around 30% during the last 5 years.

2010-2014: Armenia's Trade with the Countries of European Union (EUR, mln)

Source: European Commission, Directorate-General for Trade

Year	2010	2011	2012	2013	2014
Export	260	322	275	261	276
Import	556	645	683	717	714
Total	816	967	958	978	990

Armenia's Top Trading Partners

The Eurasian Economic Union as a block, Russia as a country and the European Union have been and remain the largest trading partners for Armenia, followed by Asia (export in 2013/2014 being USD 363,124mln and USD 484,506mln and import in 2013/2014 being USD 1,359,237mln and USD 1,429,696mln) and Americas (export in 2013/2014 being USD 187 833mln and USD 187 984mln and import in 2013/2014 being USD 292, 277mln and USD 278 892mln).

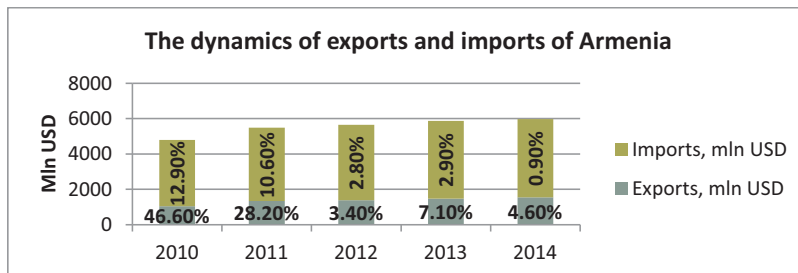
By country, according to the Customs Service of the Republic of Armenia Russia is the largest trade partner of Armenia, and following Russia in the top ten Armenian trading partners are:

Country	Export, mln USD		Import, mln USD	
	2013	2014	2013	2014
China	68, 838	170, 954	386, 021	417, 064
Germany	85, 568	158, 507	280, 919	283, 792
Iran	99, 171	82, 673	200, 221	207, 332
Turkey	1, 596	1, 494	210, 807	232, 341
USA	89, 030	87, 699	137, 558	132, 218
Italy	23, 191	34, 554	164, 418	179, 829
Ukraine	15, 228	10, 966	226, 487	201, 689
Switzerland	24, 553	13, 885	172, 528	146, 172
Belgium	131, 136	62, 412	73, 387	89, 194

Source: Customs Service of the Republic of Armenia

2.2. Foreign trade trends in Armenia by commodity groups

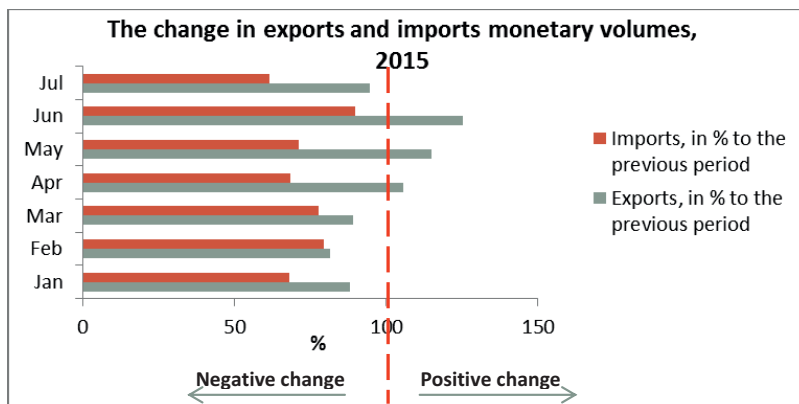
The foreign trade of Armenia has been on a steady rise since the dramatic downfall in 2009, when the country recorded 26.5% decrease in the foreign trade activities due to the global financial crisis. In the period of 2010-2014 a balanced annual growth of 6% was observed for total foreign trade volume in Armenia. The revival of exports' domain was more substantial – 10% annual growth, compared to that of imports' sector – 4%.



Source: National Statistical Service of RA (NSS)

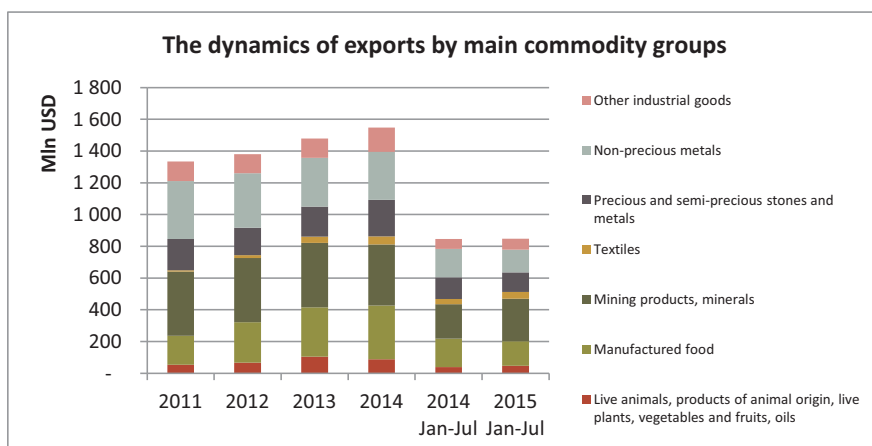
Note: Percentages in labels show annual growth rates.

The foreign trade demonstrated quite troublesome performance in 2015. With the official entry into the Eurasian Economic Union Armenia demonstrated abrupt negative dynamics both in exports and imports. In the first quarter of 2015, export activities fell by ~ 10% and imports by ~ 20%. The negative trade dynamics in this period was explained by possible discrepancies in statistical reporting. Even if the stated is true, the imports recorded continued deterioration in the next quarter, as well. Further, in July imports decreased by about 40% compared to 2014 July. The exports which have been showing signs of revival since April, again, declined by 5% in July. This was accompanied by a slight depreciation of the local currency – about 0.5%.



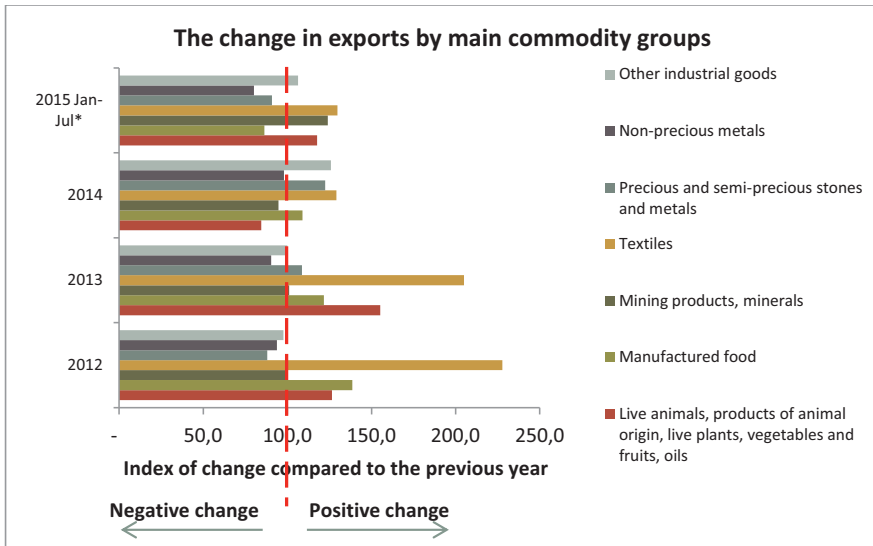
Source: National Statistical Service of RA (NSS), Author's calculations

Despite the significant fluctuations in recorded export volumes in 2015, the export structure has not changed much. The biggest export groups are food products, mining products, precious, semi-precious and non-precious metals and stones. Of these, mining products expanded their share in export basket, while others – shrank in their shares.



Source: National Statistical Service of RA (NSS), Author's calculations

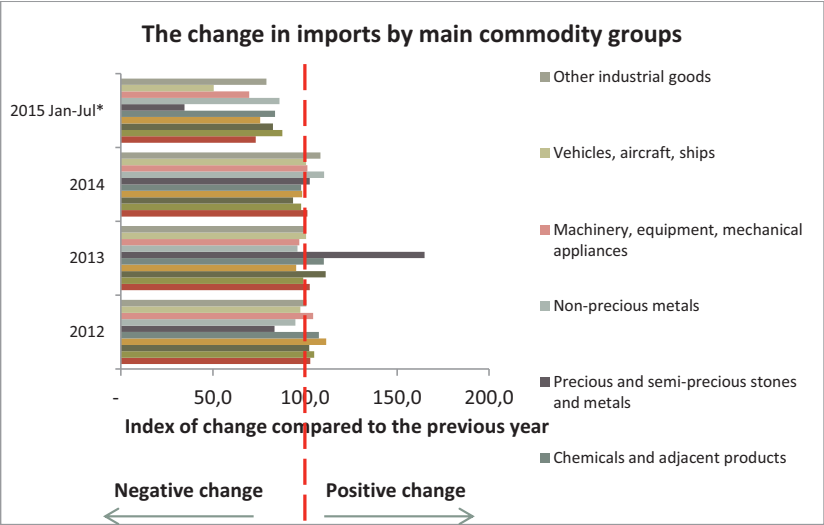
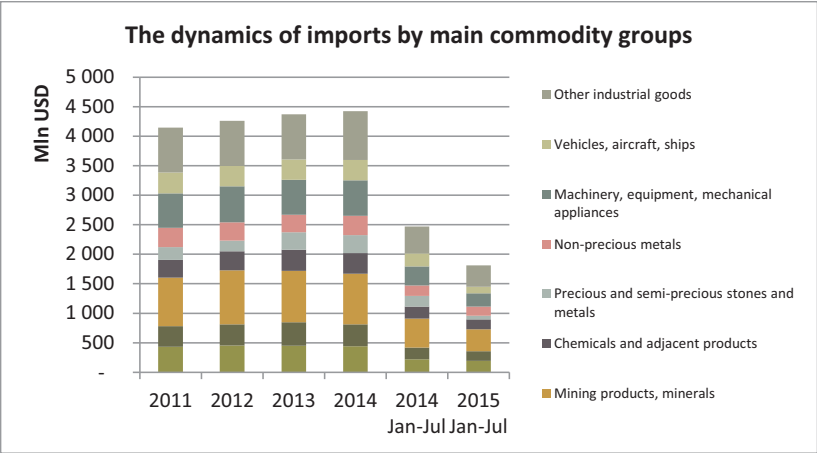
Food products, precious and semi-precious metals and stones as well as non-precious metals were the 3 groups to report negative dynamics in 2015. In the last case the export performance has been deteriorating for several years. Whereas the decline in exports of manufactured food was mainly due to decreased brandy exports at the beginning of the year.



Source: National Statistical Service of RA (NSS), Author's calculations

*Compared to 2014 Jan-Jul.

Significant decline in imports was observed by all commodity groups during January-July 2015. The imports of precious and semi-precious stones and metals, vehicles and machinery decreased by 65%, 50% and 30%, respectively. Items in all other groups experienced from 15% to 25% downfall in the same period.



Source: National Statistical Service of RA (NSS), Author's calculations

*Compared to 2014 Jan-Jul.

CHAPTER 3. NEW ECONOMIC OPPORTUNITIES FOR ARMENIA IN EEU AREA

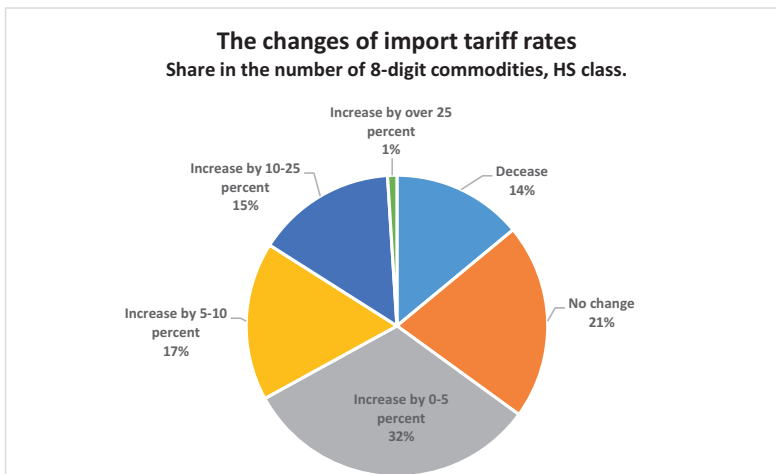
3.1. Framework of analysis

Armenia's entry in a new economic union was a ground breaking shift in the country's economic policy. The membership in the EEU is the new economic reality for the country. The first and foremost impact of such membership is expected to be open markets of the member countries and free trade among them. This implies vast market opportunities brought to member countries in single customs area where no costs imply for trading across the border within the union.

However, the real potential impact of the integration can be assessed only in comparison of Armenia's trade regime before the entry in the EEU and its current commitments within EEU.

Before January 1, 2015 Armenia had a liberal trade regime. Armenia has been a member of WTO since 2003, had free trade agreements with the majority of CIS countries and Georgia, and traded with favorable GSP regime with other significant trading partners, such as USA, Canada and EU.

This means that within the EEU Armenia gets no further advantages regarding the tariffs for foreign trade. Furthermore, Armenia has to change its trade policy regarding non-EEU countries. Customs tariffs for EEU, which were designed mainly based on Russia's trade regime (92% of the Single Tariff Rates correspond to Russia's tariffs), are much higher Armenia's average weighted tariff rates. Thus, according to a study implemented by Economic Development and Research Center (EDRC), the import tariff rates for over 65% of commodities (categorized by 8-digit HS system) will increase for Armenia.



Source: EDRC

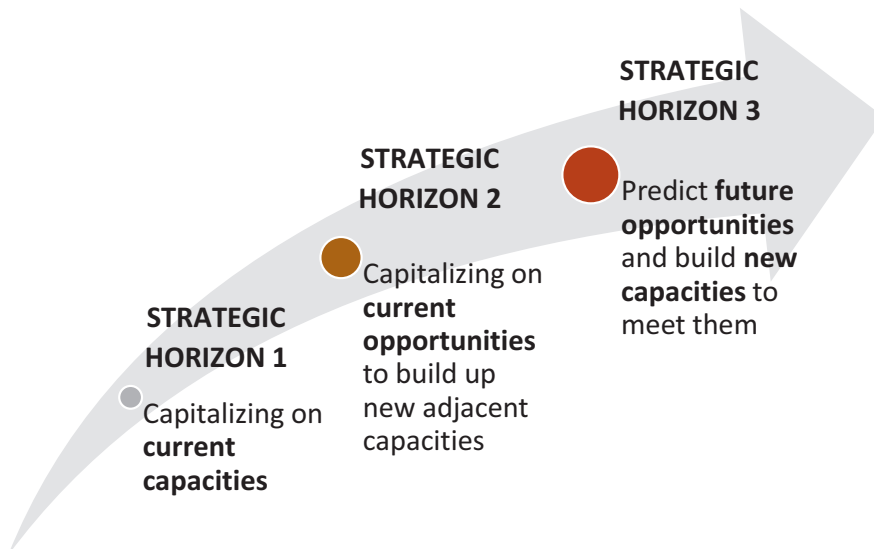
This implies that, with the entry into EEU Armenia:

- Does not benefit from deeper opportunities of free trade, as the economy was already functioning in a very liberal regime. However, even in this case the local producers were not able to use the country's trade policy in their benefit and trade regime did not intensify their access to foreign markets. It is still believed that there is a significant opportunity to ease the access to EEU countries due to the eliminated bureaucracy, procedures and required certifications. In addition, all EEU countries, except for Russia, are literally new, untapped markets for Armenia where our local producers can be positioned as a member of a single union.
- The increased import tariffs in non-EEU countries will lead to import-substitution in Armenia with the local production and with imports from EEU countries. The same will happen with other EEU countries which means that Armenian production can substitute imports from non-EEU countries in member countries.
- Other, non-trade benefits are expected to be the most long-term and plausible effects from the ties with EEU. Free capital and labor movements, as well as single state procurement domain can open up new frontiers for Armenia to attract investments and to export commodities and services which were otherwise not competitive to export.

All these imply that the outlook of Armenia within EEU is not very straightforward. Moreover, even if there are opportunities provided by the integration, they are not just given, Armenia has to elaborate a profound and forward-looking strategy first to create and then to seize new economic opportunities.

The opportunity analysis and the strategy design should be based on a phased approach to follow the logic of the integration process. If we try to generalize the prospects of Armenia within EEU we can categorize three Strategic Horizons, which differ from each other by the provided opportunities and, consequently, by the required strategies.

Strategic Horizons and mapping of Armenia's economic opportunities within EEU

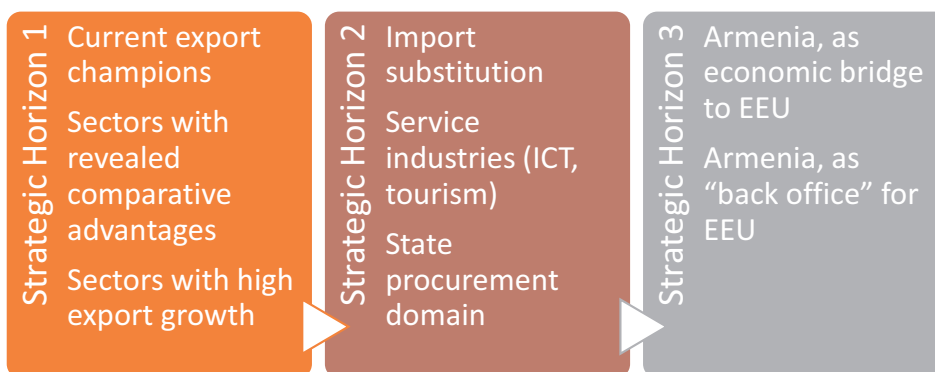


In the **Strategic Horizon 1** Armenia should focus on short-term perspectives that is to capitalize on capacities the economy currently has. In this stage the country should invest resources in the sectors that are already exporting, are export champions in Armenia’s trade portfolio and have revealed comparative advantages (compared to other sectors).

Strategic Horizon 2 is about market opportunities that currently exist in EEU, however Armenia does not have enough capacities to meet these opportunities. Two groups of sectors are distinguished in this Horizon. The first group refers to the currently existing markets in EEU countries where Armenia has some capacities to enhance or can easily build adjacent capacities and tap the markets. The second group refers to newly formed import substitution markets both in Armenia and in other EEU countries.

The most comprehensive and forward looking opportunities are drawn in the **Strategic Horizon 3**. These prospects are neither explicitly seen at present, nor Armenia has current capacities to enter in this domain. In the same time, these are the largest-scale economies with highest value added for the long-term growth of the economy. The core of the Strategic Horizon 3 should be not just reflecting but creating new economic opportunities. Activities towards attracting investments and becoming a hub and the “representative” of EEU to the external world will be the cornerstones of Armenia’s strategy in this horizon.

Strategic Horizons of Armenia’s opportunities within EEU: the target economic sectors under each Horizon



The mapping of Armenia’s opportunities within EEU reveals different growth strategy paths for the country. In some cases Armenia is given the opportunity to strengthen its positions in the existing markets and by the existing products groups (that is - currently exported), in others – it should develop strategies to market existing products in new markets (such as EEU countries other than Russia) and in most complex but promising scenario – Armenia should tap new markets with new products. Although the last option represents a longer-term outlook, it requires actions to be undertaken right away.

Armenia’s growth strategy paths for Strategic Horizons

	Existing product	New product
Existing market	Market penetration <i>Strategic Horizon 1</i>	Product development <i>Strategic Horizon 2</i>
New market	Market development <i>Strategic Horizon 1</i>	Diversification <i>Strategic Horizon 2</i> <i>Strategic Horizon 3</i>

3.2. Strategic Horizon 1

3.2.1. Champions in Armenia’s export portfolio

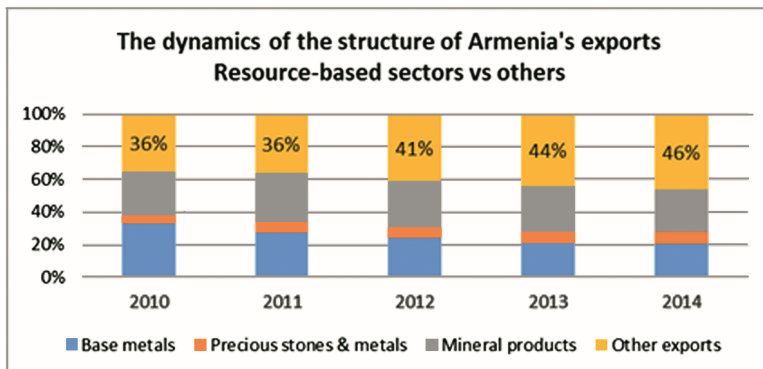
Armenia traditionally has resource-intensive exports. Resource dependency in exports is specific to countries in the first stage of export/economy sophistication.¹In this stage the economy is **factor-driven** and countries compete based on factor endowments – mainly natural resources and low-cost and low-skilled labor force. The main competition factor in this case is the price. Along to moving to higher productivity schemes, the wages in the economy begin to increase too, which means the country can no longer compete by price levels/cost advantages only. Next, the economy is in another – **efficiency-driven** stage of economic development. In this stage the economy has to invest in designing and employing more efficient ways of production and increase product quality to compete in international marketplace. The third and most sophisticated stage is the **innovation-driven** stage. The competition among the players in this stage is based on producing new and different goods not only by employing most progressive production processes but also innovating in new ones.

According to the World Economic Forum, Armenia has been moving back and forth from factor-driven into transition stage (transition from factor-driven to efficiency-driven) for a while.

Despite a significant improvement in resource-intensity indicator², Armenia still has a high share of resource based industries in its exports portfolio for a country that is landlocked, has closed borders with 2 of its 4 neighbors, and the country’s government has numerously announced about its intentions to make Armenia a knowledge intensive economy.

¹ World Economic Forum

²The share of resource-based exports in total exports.



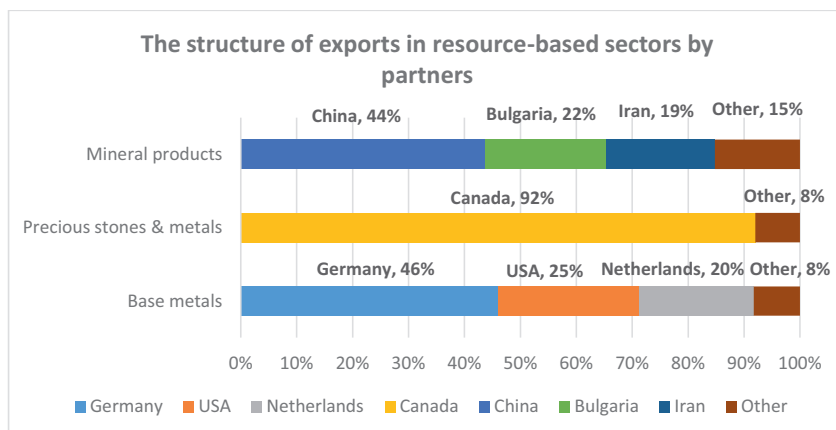
Source: UN Commodity Trade Database, Author's calculations

In addition, the export structure did not improve in favor to other sectors: the exports of natural resources just went down in monetary terms due to international prices. Also, the rapidly increasing mining and exports of gold kept the resource-intensity indicator at relatively same level.

The exports of these resources are highly concentrated in geography terms. 1-3 countries account for about 90% of exports of these commodity groups. China, Bulgaria and Iran are the main buyers of minerals from Armenia, with copper ores dominating the exports to these countries. An insignificant volume of minerals are exported to EEU countries, totaling to just 0.5% of Armenia's exports (1.9mln USD).

Over 90% of exports in precious metals (mainly gold) is exported to Canada. In addition about 4mln USD and 2mln USD is exported to Germany (4%) and Russia (2%) respectively.

The main markets for Armenian base metals – copper, iron and steel are Germany, USA and Netherlands. Again, EEU countries import negligible amount – 1.3mln USD, which is 0.4% of total exports in Armenia's base metals.



Source: UN Commodity Trade Database, Author's calculations

The exports of natural resources are not viewed in this study as a lucrative export opportunity within EEU. These industries are already mature and have a certain structure. All of the sources and mines of the natural resources are owned and controlled by foreign companies. In addition, the market prices are determined in international markets and the future outlook in these sectors depends on a wide variety of non-market, rather political factors. The only possible market opportunity for this sector (especially base metals) is developing refinery industries to export higher value added commodities. However, various due diligence studies find that setting up a refinery in Armenia is not economically sound.

This means, the mentioned resource-based sectors will not be analyzed further in this study in terms of new market opportunities within EEU.

Other than natural resources, the dominating export groups of Armenia are presented below (above 20 mln USD of exports in 2014, which is 1.5% of Armenia's exports).

Main items in Armenia's export portfolio, 2014

Commodity groups	Share in Armenia's exports, 2014	Exports value, USD, 2014
Mineral products	26.1%	389,383,148
Base metals	20.3%	302,300,014
Alcoholic beverages	11.9%	177,011,237
Diamonds	7.9%	118,017,982
Tobacco	7.8%	115,881,754
Precious or semi-precious stones, precious metals	5.9%	88,241,739
Machinery, products of engineering	3.4%	50,166,363
Textiles	3.3%	49,899,316
Fish and aquatic products	2.0%	30,516,949
Vegetables and fruits	1.7%	25,797,804
Jewelry	1.5%	21,739,954
Articles of stone, plaster, glass, etc.	1.4%	21,030,074

Source: UN Commodity Trade Database, Author's calculations

Alcoholic beverages

Armenia exported 177 mln USD alcoholic drinks in 2014. Brandy accounts for the biggest share in the exports of alcoholic beverages from Armenia. Following to the 89% percent of brandy's share, other comparably big and promising items of alcohol exports are wine – 4% and wines of various fruits other than grapes³ – 2%.

The biggest market for alcoholic beverages is Russia – consuming 80% of Armenian exports in this category. The second biggest importer is Belarus. However, the case of Belarus is a different story. It

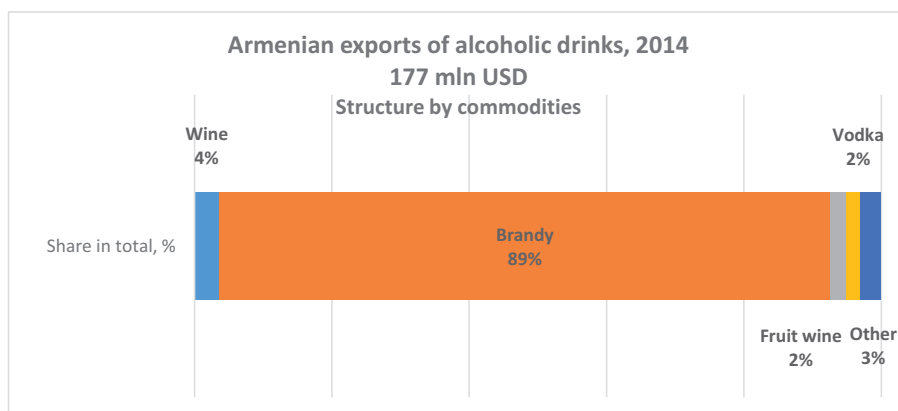
³Other fermented beverages (for example, cider, perry, mead); mixtures of fermented beverages and mixtures of fermented beverages and non-alcoholic beverages, not elsewhere specified or included.

imports raw material and manufactures brandy on site in cooperation with one of the biggest Armenian brandy manufacturing companies - Yerevan Ararat Brandy-Wine-Vodka Factory.

Thus the exports to EEU countries other than Russia are practically equal to zero.



Source: UN Commodity Trade Database, Author's calculations



Source: UN Commodity Trade Database, Author's calculations

Based on the analysis of the existing production capacities and existing markets, brandy, wine and fruit wines have the biggest opportunities for market expansion within EEU.

The exports market of Armenian **brandy** is the most mature. Armenia exports about 160 mln USD brandy in total. Russia's import market in brandy is 409 mln USD. In physical terms, Armenia is the biggest importer of brandy to Russia. It supplies Russian market with 34 thsnd tons of brandy, followed by French cognac counting up to 21 thsnd tons. The two biggest foreign brandy suppliers, however, play in totally different market segments. France is positioned in high-price segment (average trade value per kg – 10 USD). Whereas, Armenia sells most of its products in medium-price segment (average trade value per kg – 4 USD). Further market expansion in Russia is possible in 2 main frontiers:

- Tap and expand into the high-priced brandy segment and compete with French cognac, with 214 mln USD market volume.

- Address trade diversion opportunities and expand into lower-priced segment of non-EEU suppliers. As of 2014, Ukraine, Georgia, Azerbaijan and Uzbekistan supplied 17 thsnd tons of brandy to Russia with 54 mln USD trade value, comprising 13% of Russian imports. The average price of brandy imported from these countries is lower compared to Armenian brandy by 20%.⁴ Currently, the membership in EEU may lead to higher price competitiveness of Armenian brandy in the Russian market. In this case, Armenia can also compete in lower-priced market segments and account for higher share in the market.

The brandy import markets of Kazakhstan and Kyrgyz Rep. are nascent. Together they import just about 4 thsnd tons of brandy at 18 mln USD. In addition, Armenian brandy is less competitive in these markets due to high prices caused by high transportation costs. In brandy imports market of Kazakhstan Armenia competes with Georgia and Moldova. The average price of brandy supplied from these countries is 2.8-3.1 USD per kg against 5.5 USD per kg for the Armenian brandy.

An additional 33 mln imports market of brandy exists in Belarus. Moldova counts for half of this market supplying brandy at 5 USD per kg, whereas Armenia's brandy in the same market is priced at 9 USD per kg.

Thus, the other 3 EEU countries (except Russia) are presented with just ~50mln USD brandy imports markets. This is not a significant expansion opportunity for Armenian brandy, given that the country's production does not have price competitiveness in these countries. Rather, Armenia can export brandy without packaging to be bottled in these markets on site.

The situation in **wine** imports market is reverse to that of observed in brandy market. The imports of wine in EEU market is immense and comprise approximately 1.3 bln USD and 726 thsnd tons (Russia's share is 90% in this). As of 2014, Armenia exported just 3.7 thsnd tons of wine at 6.3 mln USD trade value.

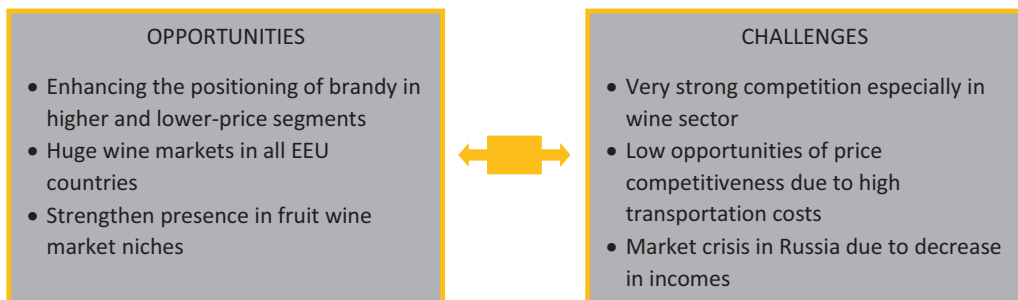
Fruit wine is a niche segment in the total market of alcoholic drinks. Armenia's exports in these category is almost equal to wine exports – 3.9 mln USD in 2014. EEU imports of wines made of various fruits (other than grapes) comprise 84 mln USD. Lithuania, Moldova and Italy are the biggest importers in this segment. Russia, itself is a big producer and exporter of fruit wines.

	Russia	Kazakhstan	Belarus	Kyrgyz Rep.
Total imports of brandy	408.7	16.4	33.1	1.7
France	52%	33%	0%	24%
Armenia	32%	11%	20%	10%
Georgia	5%	30%	11%	0%
Moldova	0.4%	17%	47%	9%
Uzbekistan	1.2%	0%	0%	49%

⁴ Trade value per 1 kg of imports is taken as a proxy for average prices.

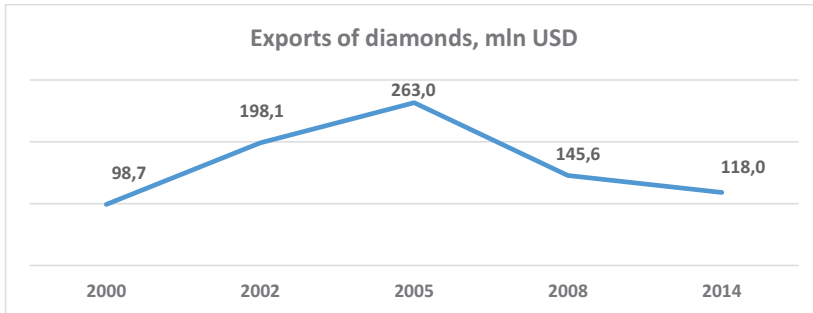
Others	10%	9%	23%	8%
Total imports of wine	1,143	55.7	65.3	4.4
Italy	29%	18%	1%	13%
France	21%	14%	1%	11%
Georgia	14%	31%	11%	10%
Armenia	0.41%	0.02%	0.49%	0%
Moldova	1%	26%	51%	37%
Latvia	0%	0%	15%	0%
Others	34%	11%	21%	42%
Total imports of fruit wine	78.5	3.1	2.1	0.1
Lithuania	55%	0%	15%	0%
Italy	19%	1%	0%	0%
Armenia	2%	5%	0%	0%
Moldova	0%	78%	19%	34%
Russia	0%	12%	25%	51%
Estonia	0%	0%	29%	0%
Others	24%	4%	26%	15%

Source: UN Commodity Trade Database, Author's calculations

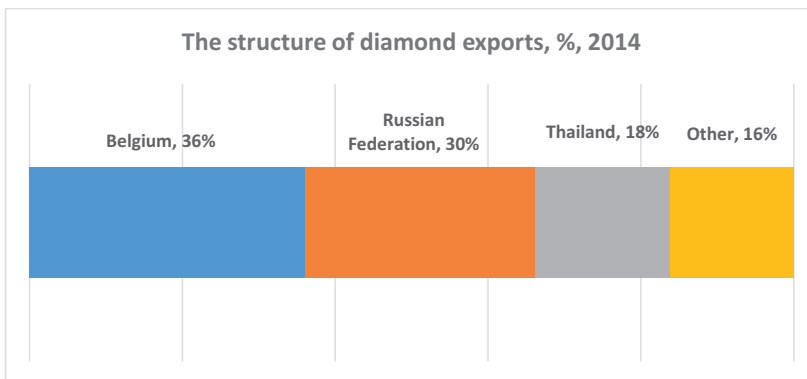


Diamonds

Diamonds are another significant part of Armenian exports. It is not calculated in the country's resource-intensity indicator, as it is not based on the extraction of Armenia's own natural resources. The country imports raw diamonds and specializes on cutting and polishing of the medium-sized diamonds. The history of Armenia's diamond cutting industry goes back to the Soviet Union where Armenia was one of the biggest centers of diamond processing. The country set up significant facilities of processing and gathered high reputation in processing medium-sized diamonds. In the modern history of Armenian diamond industry, the sector experienced upsurge in 2002-2003 when a few international companies entered the market and also Armenia signed an intergovernmental agreement with Russia about beneficial conditions and certain quota in the procurement and processing of raw diamonds. However, with the liberalization of Russia's diamond market, the cooperation with Armenian processors decreased drastically.



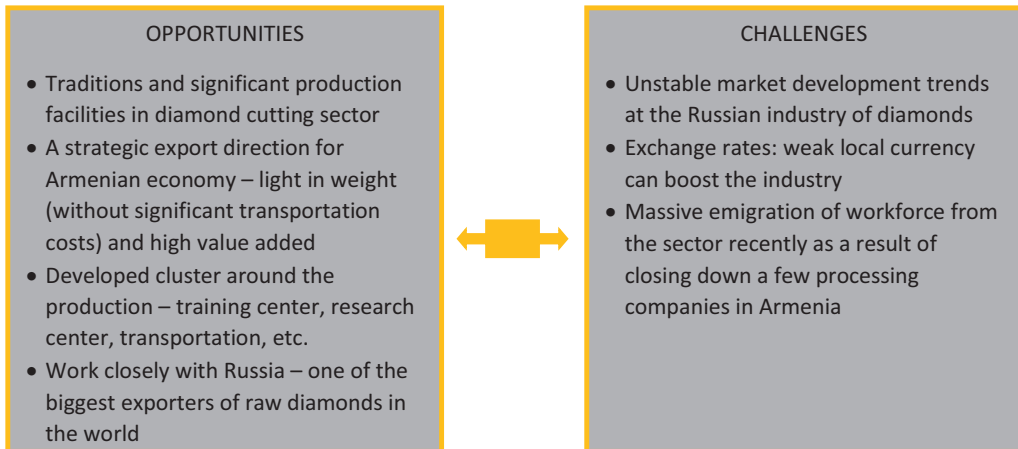
Source: UN Commodity Trade Database



Source: UN Commodity Trade Database

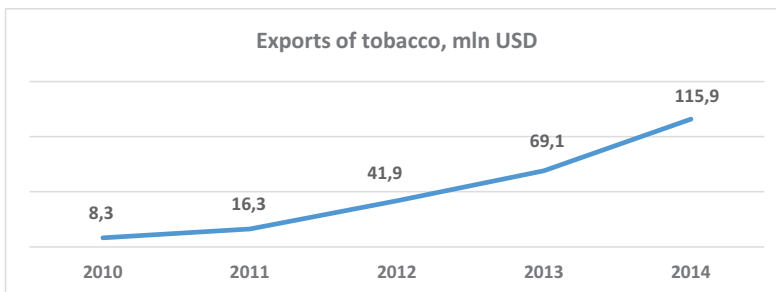
In 2014 another intergovernmental agreement between Russia and Armenia eliminated the 6.5% export tariff when importing rough diamonds from Russia to Armenia. Given the labor cost advantages of Armenia compared to Russia and low transportation costs of diamonds, the local diamond cutting industry can be quite attractive to cooperate with. However, despite the competitive advantages against Russia, Armenia is positioned less competitively compared to world leaders in diamond cutting and polishing – India and Asia. The labor cost is the biggest component in diamond processing. Whereas in Armenia labor costs are, of course, higher compared to Asian countries.

However, Armenia’s diamond cutting industry has solid traditions and is positioned in higher-value added medium-sized diamonds cut, whereas Asian countries mainly work with small diamonds. The work of Armenia’s cutters is graded with “Excellent”.

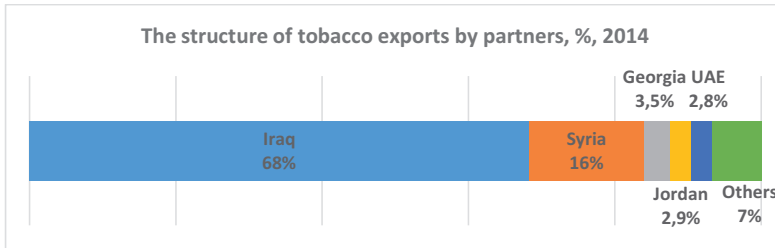


Tobacco

Tobacco is a recent emerging exports industry. With over 90% average annual growth rate the industry is the fastest growing exports commodity in Armenia. Iraq is the biggest consumer of Armenian tobacco and is responsible for its rapid growth. The supplies to Iraq have been consistently growing and, according to main producers, have a vast potential for further expansion in this market. Other than Iraq, Armenian tobacco has been successfully introduced to other Middle Eastern countries, as well. In 2015 about 25 mln USD cigarettes were exported to Syria, Jordan and UAE. In addition, 10 mln USD was sold in Georgia, Russia and Turkmenistan.



Source: UN Commodity Trade Database



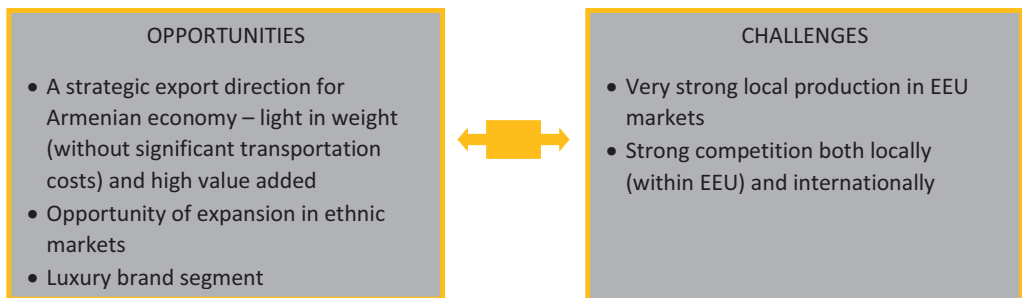
Source: UN Commodity Trade Database

All EEU countries, except for Kyrgyzstan have big local tobacco industries. Russia specifically is a big exporter of cigarettes, the exports of which has grown consistently up to 560 mln USD in 2014.

The EEU countries are in the same time big importers of cigarettes. As of 2014, the total imports in the 4 EEU countries (except Armenia) was over 300 mln USD, 30% of which was imported to Russia. 63% of imports to Kazakhstan, Belarus and Kyrgyzstan was supplied by Russia. In Russian market Armenian tobacco has been marketed and consumed by the segment of ethnic Armenians so far. Despite the strict competition and developed local industries, the market opportunities for this commodity are not insignificant for Armenia. In EEU, Armenia can focus on higher-priced luxury segment of branded cigarettes such as produced by Cigaronne SPS.

Exports of tobacco have a special strategic importance for Armenia, given the light weight and high value added of the commodity.

Source: UN Commodity Trade Database

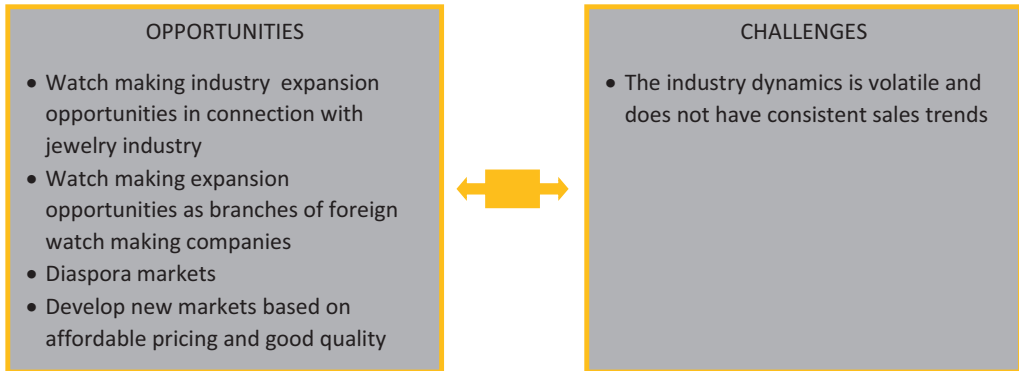


Machinery, products of engineering

The cluster of engineering products is among the most significant Armenian exports, however, it is also the most volatile one in terms of export dynamics. So far it has been dependent on discrete partnership opportunities, such as the export of different parts of aircraft: during 2011-2013 Armenia exported over 90 mln USD in this category, which dropped to just 2 mln USD in 2014.

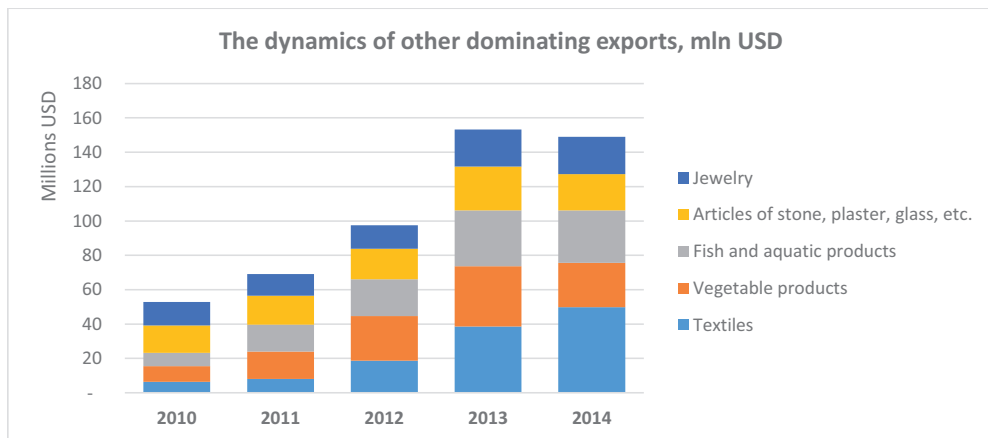
As of now the biggest exports in this cluster are clocks and parts of watches (36%), including cases for watches which is more a jewelry product. The watch making sector has experienced consistent and significant growth in Armenia backed by the participation of foreign watch making companies (in most

cases owned by people with Armenian origin) launching operations in Armenia. The growing industry urged Armenian Government to include it in the most prioritized economic sectors and design a develop strategy in 2013. As of now the exports is mostly based on Diaspora markets, however the prospects are positive for other non-diaspora markets within EEU as well, due to affordable pricing and good quality of Armenian watches.



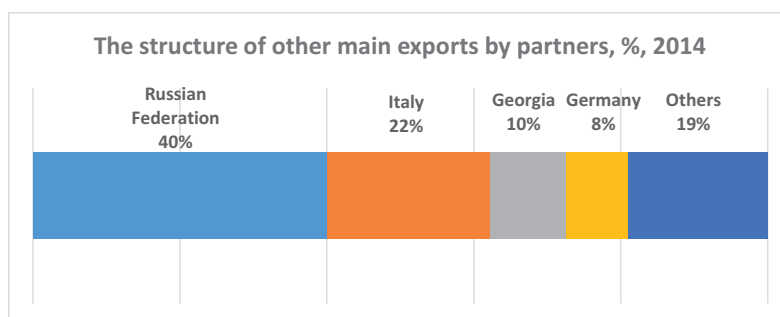
Other main export sectors

The other sectors with significant shares in Armenia’s export portfolio are textiles, fish and aquatic products, vegetable products, jewelry, as well as articles of stone, plaster, glass, etc. These clusters together 10% of Armenian exports and grew consistently at an average annual rate of 30% during 2010-2014.



Source: UN Commodity Trade Database, Author's calculations

The main trade partners by the selected commodity groups are Russia, Italy, Georgia and Germany.



Source: UN Commodity Trade Database, Author's calculations

Armenian textile production is mainly sold in European countries – Italy, Germany and France, as the local textile manufacturing companies mainly work on large-scale predefined contracts with European companies.

Russia accounts for the lion's share in the exports of agricultural products, namely fish and vegetables products.

The cluster of building materials (articles of plaster and stone) has quite positive prospects of development. However, due to the heavy weight of commodities, Armenia's closest neighbor-Georgia, has so far been the main trading partner in this market. In order to expand its exports Armenia needs to invest in light-weight construction materials.

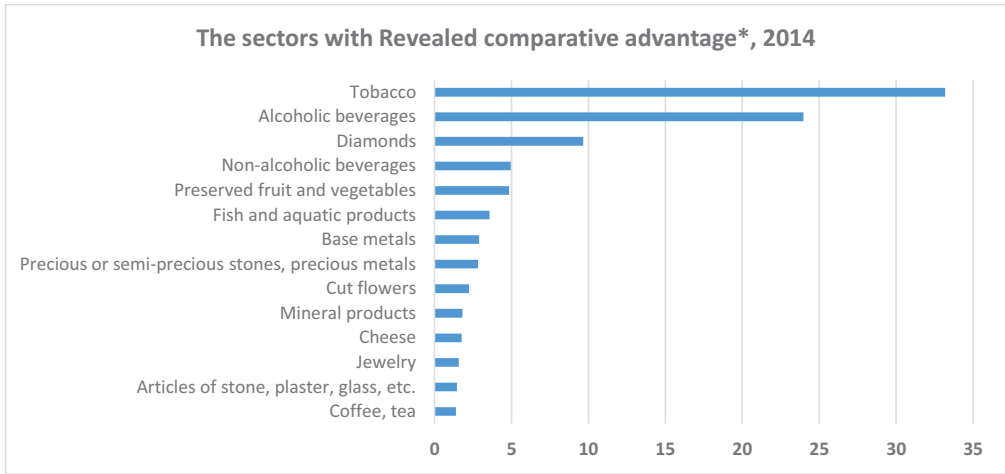
3.2.2. Sectors with revealed comparative advantages

The next target group within the Strategic Horizon 1 are clusters with revealed comparative advantage (RCA) for exports. The RCA, also called Balassa index⁵, is an index which shows the levels of trade specialization of a specific country in a specific commodity/cluster.

In terms of RCA a country is considered to be specialized in the exports of a commodity if the weight of the product of the country's exports is higher than its weight of the exports of the world. A country has revealed comparative advantages to export products for which RCA indicator is higher than 1.

If we exclude previously discussed sectors, non-alcoholic beverages and preserved food and vegetables are the sectors with high interest in the list of Armenia's sectors with RCA for 2014.

⁵Balassa, Bela; Marcus Noland (1989).

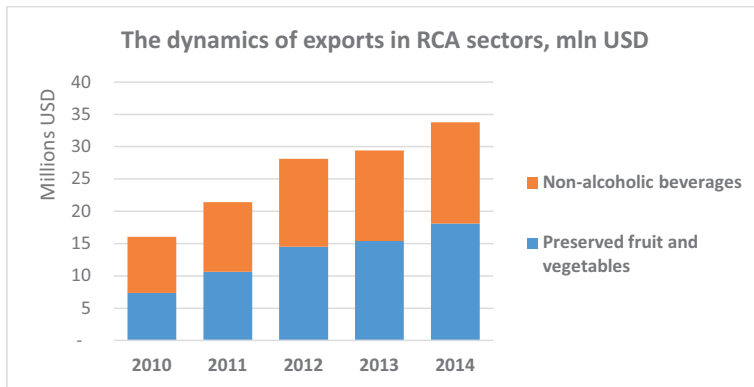


Source: UN Commodity Trade Database, Author's calculations

*Sectors where the index of RCA is greater than 1.

Non-alcoholic beverages and Preserved food and vegetables

These sectors together account for 33 mln USD exports. These are among the most dynamic growing sectors with average annual growth rate comprising 20% in the period of 2010-2014.



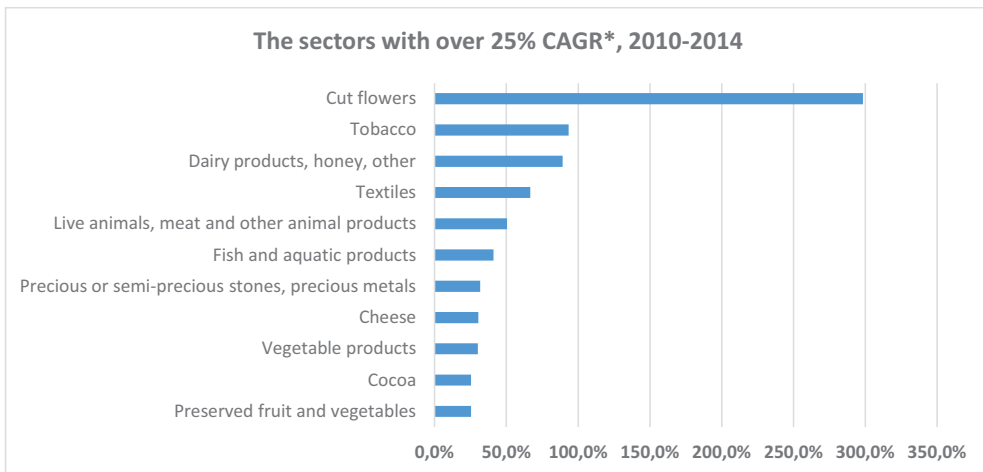
Source: UN Commodity Trade Database

Despite the impressive growth rates, the sectors do not stand out with high competitiveness. The main current markets are ethnic Armenians in Russia (79%) and USA (6%). The sector of preserved fruit and vegetables is highly based on manual technologies and lacks progressive automated production facilities. This limits the production capacities, increases the production costs and limits the opportunities of international quality certifications.

3.2.3. Sectors with high export growth

The clusters with high growth performances are strategic directions with high level of attractiveness for investments. Even if these sectors do not dominate in the current export portfolio, they are on the track of impressive development which indicates the existence of necessary premises and market factors which can be harnessed further.

Again, if we exclude already discussed sectors, the clusters of cut flowers and dairy and cheese can be highlighted among the sectors with strong growth performance.



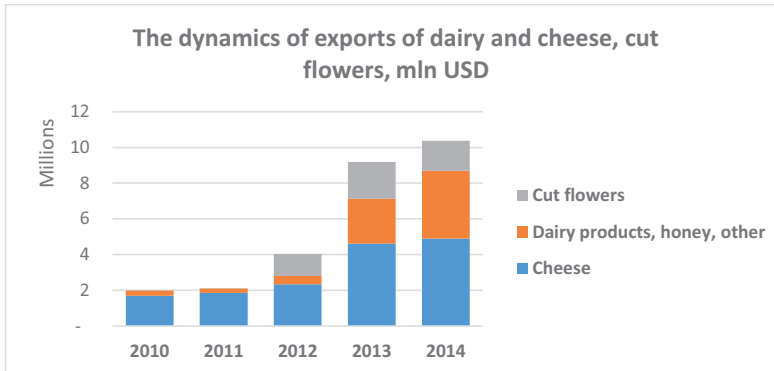
Source: UN Commodity Trade Database, Author's calculations

*Compound annual growth rate

Dairy and cheese, cut flowers

Both of the sectors have small but consistently growing export bases. 99% of dairy and cheese is exported to Russia. Armenian cheese has a quite stable market in Russia. However, the opportunities of rapid expansion are quite limited for cheese, as the local supply base is highly fragmented and inconsistent.

The increasing exports of cut flowers signal the attractive prospects not only in the market of this particular commodity, but also the products of greenhouses in general. The current export markets of cut flowers are Russia (74%), as well as Georgia and Belarus.



Source: UN Commodity Trade Database

3.3. Strategic Horizon 2

3.3.1. Import substitution

Insert: trade creation and trade diversion effects within customs unions

In free trade environment countries trade with partners which provide the most competitive products. In this case the competition is based on market factors: comparative advantages in producing goods and services. In international competitive market countries specialize in exporting commodities that they produce with higher productivity and, consequently, lowest prices. Importing countries, of course, choose to import from lower-cost suppliers which capitalize their cost advantages in production to lead the international markets with competitive pricing.

However, when customs unions are created, the trade flows and their directions are driven by non-market factors as well, such as different tariffs for union members and other countries. The countries within the free trade area gain competitiveness due to their lower (or zero) tariff rates. Whereas the products from nations that are originally cost efficient become more expensive to import due to higher tariffs. Thus, inefficient producers become protected and favoured against more efficient ones by the customs regulations of their customs union.

J. Viner⁶ differentiates two possible effects in the result of forming a customs union and changing the game rules. *Trade creation* effect is caused when free trade and elimination of tariffs within the member countries leads to decrease of production costs and lowers the prices of commodities produced within the customs union. This will result into higher demand for these products in general, and bring to extra trade created.

Trade diversion effect does not increase the consumption of the products. It just redistributes the existing market shares and changes the import structure in favor to the members of the custom union which gain price competitiveness compared to non-member countries due to tariffs.

⁶The Customs Union Issue, 1950

The perspectives for trade creation effects within EEU to take place for Armenia are very much blurred as of now. Given the existing economic trends, the ongoing and strengthening crisis signs, there is not much hope for increasing consumption and observing trade creation effects within EEU.

In the same time, the possible trade diversion effects are quite tangible for Armenia. The trade policy imposed by EEU regulations has high level of protectionism. This means that imports from non-EEU countries are or will become very expensive, leading to extensive import substitution opportunities.

The local producers should build their strategies to adjust their production capacities to address import substitution opportunities in 2 directions:

- Substitute imports of non-EEU countries to Armenia,
- Substitute imports of non-EEU countries to other EEU members – Russia, Kazakhstan, Belarus and Kyrgyzstan.

The assessment of the opportunities for import substitution should be done carefully: in many cases the increased tariffs refer to input factors, which may make impossible for local producers to gain cost advantages compared to importers.

Import substitution in Armenia

The import substitution effect will most probably take place for the commodities, which:

- Have high share in total imports to the country,
- Are now mainly imported from EEU countries,
- Are subject to biggest changes in customs tariffs,
- Have traditions/resources/capacities to be produced locally.

The filtered list of commodities defined by the mentioned criteria is presented below.

Name	Import, 2014, USD	Range	Year when the EEU tariff comes into force
Meat and edible offal of poultry meat	40 mln	10-25	2022
Sausages and similar products, of meat, offal or blood	7 mln	5-10	2015
Spirits, liqueurs, other spirit beverages, alcoholic preparations	35 mln	>10	2015
Cigarettes	43 mln	10-25	2015
Medicaments not mentioned elsewhere	83 mln	5-10	2015
Furniture and parts thereof	20 mln	>10	2015

Source: UN Commodity Trade Database, EDRC, Author's calculations

Although Armenia negotiated a grace period until it moves to new tariffs, however, even if it happens in 2022 the economy should build up industries to accommodate its own local demand in the mentioned directions.

Import substitution in other EEU countries

The discussed effect of trade diversion is expected to be observed in the markets of EEU countries, as well. The Single Customs Tariff adopted for Eurasian Customs Union was mainly based on the existing trade tariffs of RF. In addition, Kazakhstan and Belarus has moved to the Single Tariff for several years now. This means that there are no abrupt changes in import tariffs for these countries which are expected to significantly affect their international trade trends.

However, at present there are immense trade diversion opportunities which are more associated with current geopolitical situation and Russia's external policy and its diplomatic relationships with different countries.

Russian embargo on imported products

In March 2014 EU, USA and other G7 countries announced about their decision to apply economic sanctions against Russia (mainly in military, energy, and financial sectors) which was their response to Crimea conflict and Russia's participation in it.

Russia had an immediate and aggressive response to this. In the summer of 2014 the Government of RF announced about a massive embargo on the import of a number of commodities from countries applying sanctions towards Russia. The list of commodities and commodity groups under embargo included:

- Different types of meat – fresh, chilled or frozen; meat of bovine, pork and poultry;
- Different types of fish and seafood;
- Milk and dairy (except for special lactose-free categories);
- Vegetables, fruits and nuts (except for very few commodities);
- Sausages and other processed meat products;
- Various food products.

The embargo covered EU countries, USA, Canada, Australia and Norway.

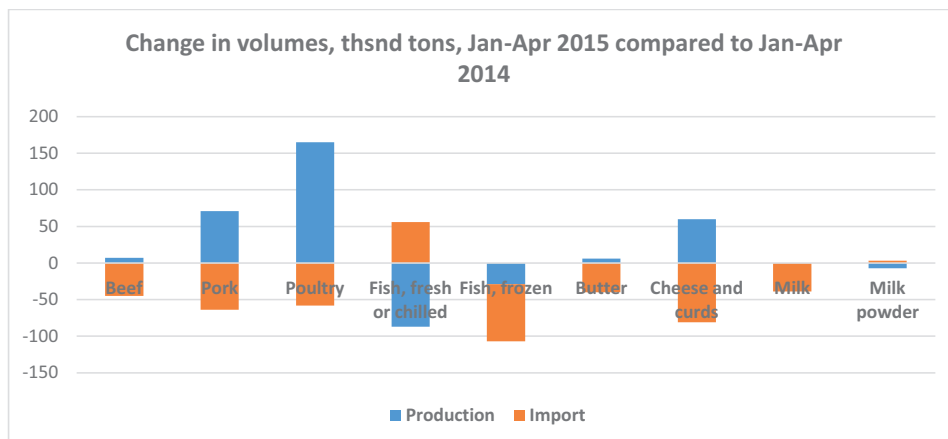
The RF Government backed up its decision by the expected import substitution effect and by the enhancement of local agricultural and food production industries in the result. However, building the local industries to meet the local demand requires 3-5 years, at least in some agricultural sectors. What happened in the short-term was just switching from one importer to another. No significant increases in the local production were documented, instead:

- Russia began to trade with less competitive partners. The meat supplied from Australia (beef steaks) and USA (poultry) was replaced by supplies from Uruguay, Paraguay, Argentine, Brazil and CIS countries.
- Belarus significantly increased its share in dairy imports to Russia.

- Both local suppliers and importers artificially increased their prices leading to unjustified inflation throughout the economy. In the result, the local market began to consume lower quality products for higher prices.
- Contraband trade became widespread. European producers easily found ways to resume their supplies to Russian market. The main means of illegal imports are reporting the commodities under other groups (such as reporting dairy under lactose-free dairy) and fraud in the country of origin of products (such as European products repackaged as Belarussian).

As already stated the decision about embargo was reasoned almost 100% by political factors and for national security reasons, as a response to sanctions applied to Russia. The recent Paris attacks and Russia's participation in the Syria's conflict resolution gave a new start to the discussions about the possible withdrawal of economic sanctions against Russia. EU is under the pressure of its producers who demand to revive economic relations with Russia. In addition, the emerging military alliance with Russia in fighting ISIS in Middle East, highlights potential changes in policy towards Russia. However, USA recently announced about its extended list of sanctions and some EU politicians also announced that there is no reasoning to review sanctions against Russia, as it did not meet the defined requirements to resolve Crimea conflict.

After nine months of the embargo the situation in Russian market was different by commodity groups. In a number of cases the local production increased substantially to cover the decline in the imports. However, this was not the case in general. In total the import and production volumes decreased by 160 thsnd tons in January-April 2015 compared to the similar period of 2014 (vegetables and fruits are not calculated). Thus, there is a substantial deficit almost on all markets of embargoed products.



Source: Analytical center by the Government of RF, August 2015

Sanctions against Turkey

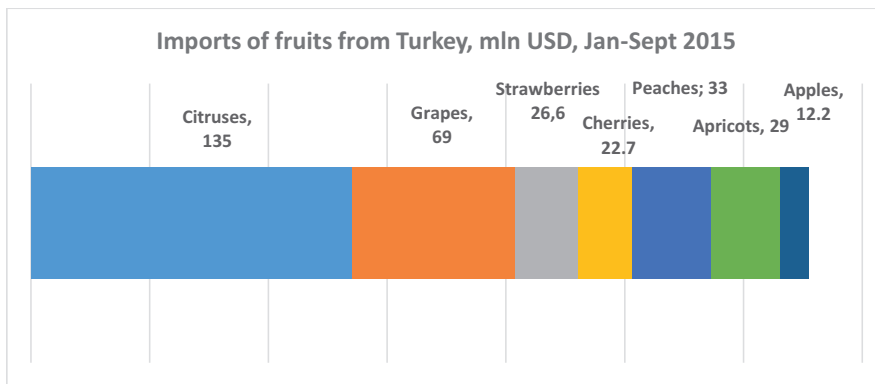
Russia announced about its intentions to design a list of sanctions and limitations regarding partnership with Turkey, after the latter crashed a Russian military aircraft.

The sanctions will include:

- Limiting the activities of Turkish companies in Russia and Russian companies in Turkey;
- Embargo on the import of Turkish products to Russia;
- Reviewing the visa regime for Turkish citizens and limiting tourism flows to Turkey.

The list of products under embargo is not published yet. However, according to the official announcements it will first hit agricultural products – particularly fruits and vegetables. In 2014 Turkey exported 1.8 bln USD⁷ of agrarian and processed food products to Russia, which comprised 4.3% of Russia’s imports in this category.

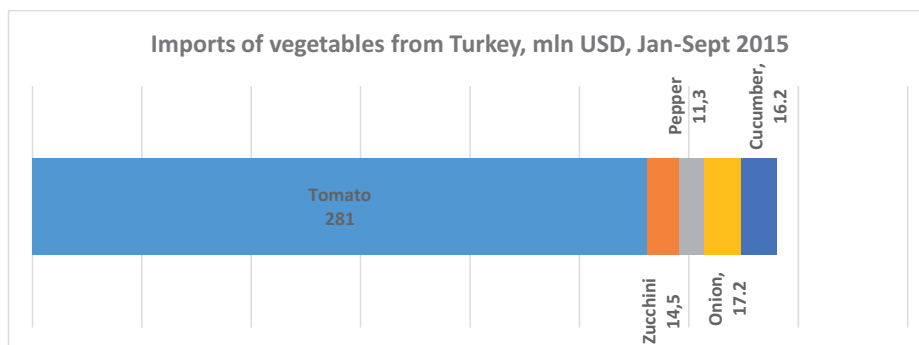
Only in the first 3 quarters of 2015 Russia imported ~750mln USD fruits and vegetables from Turkey. The dominating fruit exports are citruses -135mln USD, grapes – 69mln USD.



Source: Federal Customs Service of RF

Turkey is also the leading importer of tomatoes to Russia, accounting for half of the total tomato imports to Russia. In 2015 Turkey supplied Russian market with over 290 thsnd tons of tomatos, summing up to 280 mln USD.

⁷Federal Customs Service of RF.



Source: Federal Customs Service of RF

It is noteworthy that the imports from Turkey increased by over 30% only after the embargo of Russia against European countries.

As of now the decision of embargo refers to fruits and vegetables; the possible limitations covering industrial products are discussed too. Turkey is a big supplier of textiles (290 mln USD in Jan-Sept 2015), plastics (166 mln USD in Jan-Sept 2015) and constructions materials (41 mln USD in 2014).

The travel and tourism sector has been considered to be responsible for the strong ties between Russian and Turkish economies. According to estimations about 4.5 mln Russian tourists visit Turkey annually. The total revenues of Turkey in this industry accounted for roughly 10bln USD annually.⁸

Sanctions against Ukraine

In August 2015 the Government of RF declared the extended list of countries imports from which are under embargo. The new list included Albania, Iceland and Montenegro. A special decision was made regarding Ukraine. It was announced that if the country validates the free trade regime with EU, under the economic part of the EU association agreement, it will be included under the embargoed countries for Russia. According to estimations, Ukraine's entry into free trade zone with EU will cost 1.6bln USD loss for Russia. Whereas, the counter-response of Russia –closing its market for Ukraine, will cost 600 mln USD only in 2016.

As of now both Ukraine and, consequently, Russia have announced their final decisions: Russia is closing its borders for the imports of predefined set of products of Ukrainian origin since January 1, 2016.

Preparing to this situation both of the counterparts have been decreasing their dependency on each other. As of Jan-Sept 2015 the imports of agrarian and processed food products decrease to 3.2% of Russia's imports in these categories. Still, the recently declared embargo refers to significant trade volumes. Only in the first 3 quarters of 2015 Ukraine exported 20.5 mln tons of pork, 15.3 mln tons of bovine meat, 7 mln tons of vegetables, 874thsnd tons of curds, 40thsnd tons of milk and 20thsnd tons of butter.

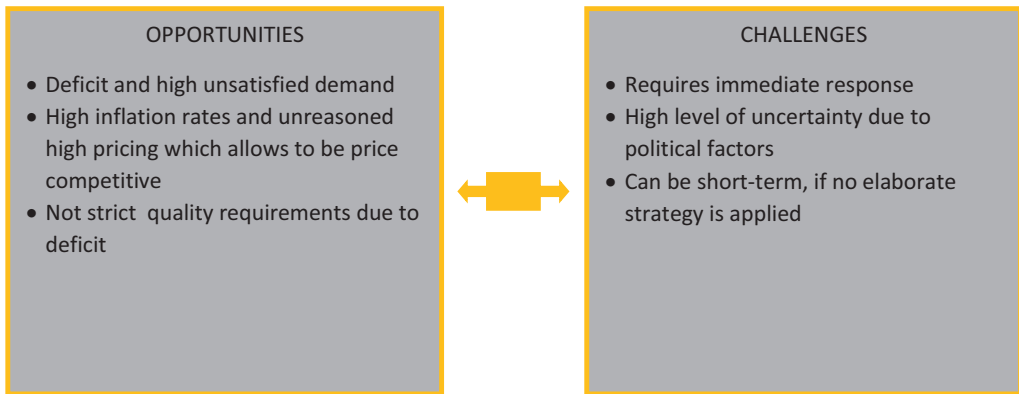
This opens up immense import substitution opportunities for other suppliers.

⁸Federal agency of tourism – Rostourism.

Sanctions towards tourism to Egypt

After a tragic crash of a Russian plane Egypt's Sinai Peninsula, the Russia decided to cut off all travel and tourism flows to Egypt. Whereas the latter was the second most popular tourist destination for Russians (after Turkey). In 2014 over 3mln⁹ Russians visited Egypt as tourists, totaling to 2.5bln inbound tourism industry for Egypt. This decision, backed with security issues, is a major slap against Egypt's tourism sector. However, the negative impact is not less for Russia too. According to the Russian Association of Travel Agencies, about 140,000 package tours to Egypt were canceled which were presold for the coming holiday season.

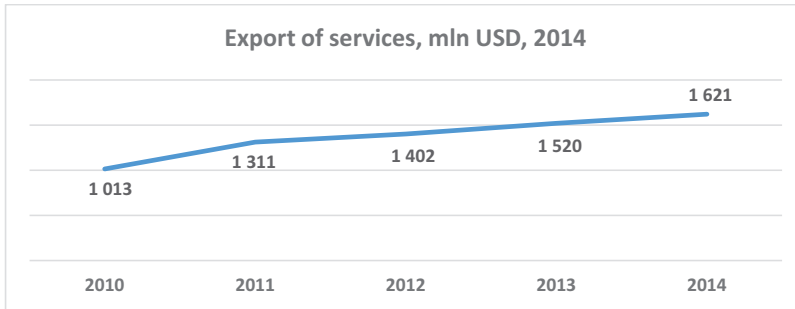
The described import substitution opportunities can be groundbreaking for Armenia. Although this sector is very volatile and depends on non-economic and unpredictable political factors, a quick response to the situation can build and enhance a whole export industry. The markets experiencing deficit is much easier to enter. Once in the market, the Armenian exporters can further expand their presence.



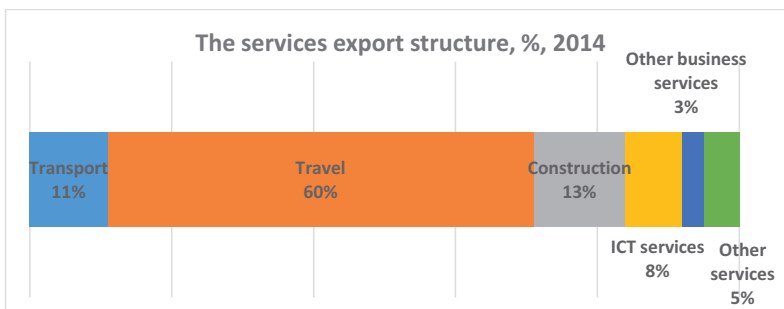
3.3.2. Service industries

The exports of services are on steady development track in Armenia. According to the World Bank's World Development Indicators database Armenia exported 1.6 bln USD services in 2014. The exports industry has increased by 12% on average annually since 2010. Tourism and travel industry accounts for the largest share in the Armenian service exports.

⁹ Bloomberg



Source: WB WDI database



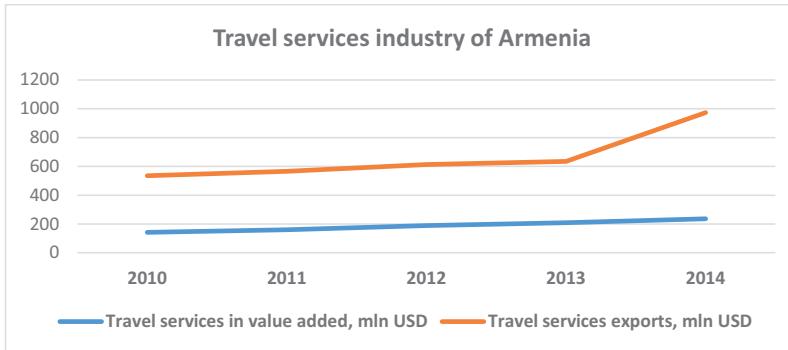
Source: UNCTAD statistical database

Tourism

According to UNCTAD statistics, Armenia exported 980mln USD travel¹⁰ services in 2014, which doubled from the 2013 indicator. The number of international tourists (as defined by UN WTO) visiting Armenia reached ~1.2 mln in 2014.¹¹

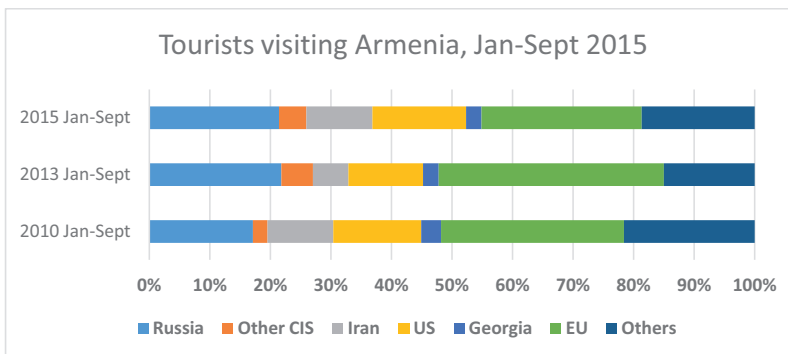
¹⁰ Defined as goods and services acquired by non-residents in Armenia.

¹¹ NSS



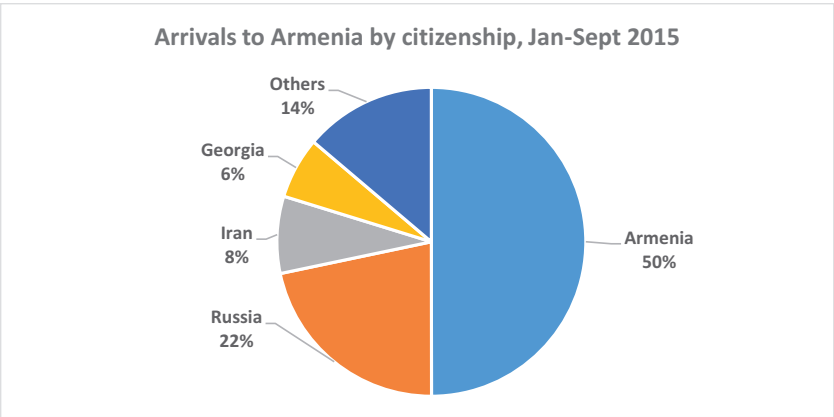
Source: NSS, UNCTAD statistical database, WB WDI database

The incoming tourists from Russia are the fastest growing tourism sector in Armenia – with 18% average annual growth rate since 2010.



Source: NSS

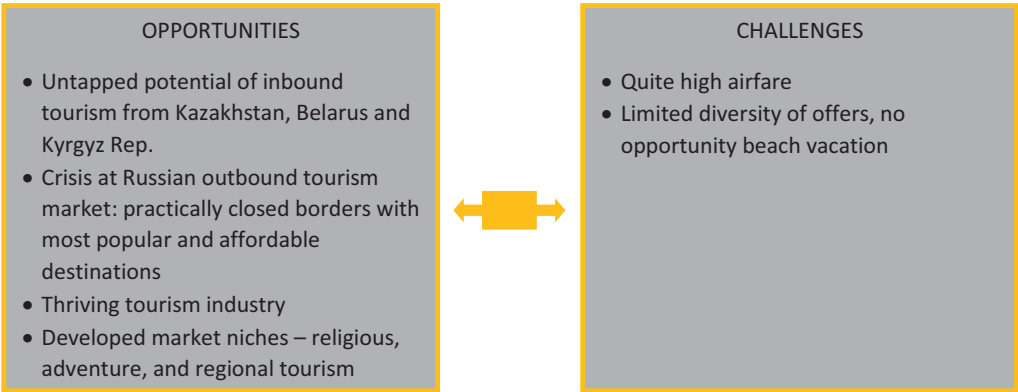
In addition, according to a recent study of NSS, if we take out the ethnic Armenians visiting the country as tourists, visitors with Russian citizenship comprise the biggest group in arrivals to Armenia.



Source: NSS

The prospects of development of tourism industry are quite promising within EEU. Other than Russia, tourist flows from EEU countries to Armenia are practically equal to zero. A few factors can significantly boost tourism growth from these countries:

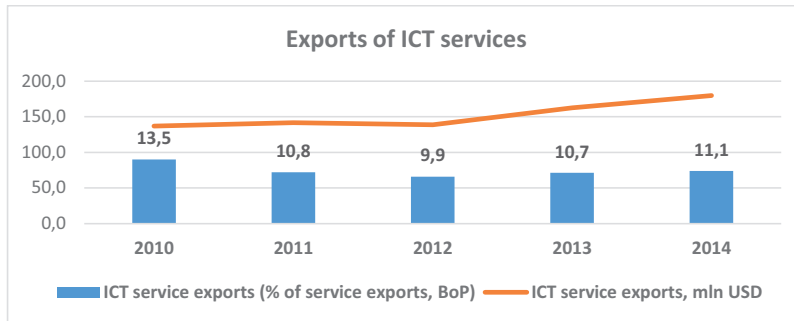
- The increased country branding just due to the entry of Armenia into EEU. Now that Armenia is in the same economic union, many citizens of other EEU countries will find it psychologically more acceptable and easier to travel to Armenia.
- The increased business activities will increase the number of business travels within EEU countries which will lead to leisure tourism too.
- The current geopolitical situation, Russia’s tense relationships with the most popular tourist destinations among Russians – EU, Turkey and Egypt, affected the outbound tourism in the country largely. The next available destinations are geographically much further and are priced much higher. This is a good time for Armenia to seize the potential of Russian inbound tourism to Armenia.



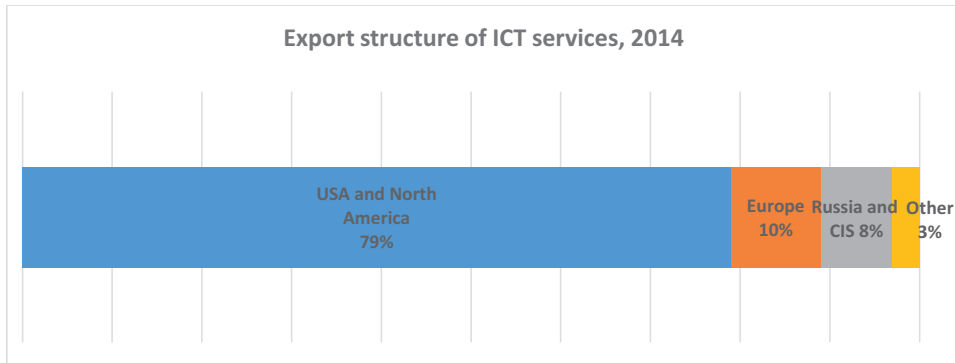
ICT services

ICT is among the most sophisticated and high-growth sectors of Armenia, which is far from saturation, as it operates in global marketplace and has no physical borders limiting the exports of IT services.

As of 2014 the exports in this sector comprised 180 mln USD which is 11% of the total service exports and is comparable to brandy export industry in its scale. USA and North America account for the lion's share in these exports.



Source: WB WDI database

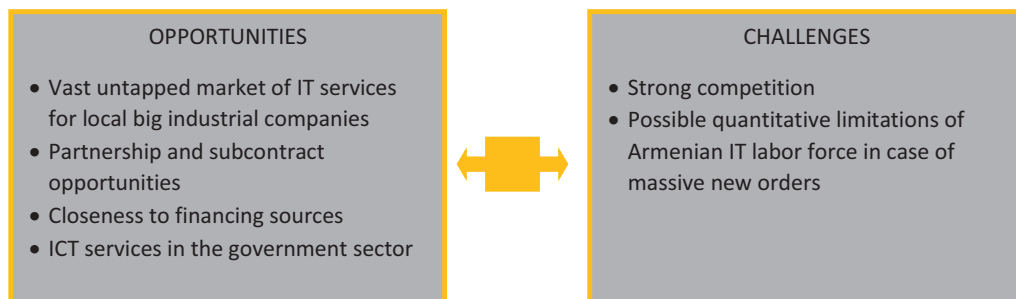


Source: "Information and telecommunication technologies sector in Armenia; 2014 state of industry report", Enterprise Incubator Foundation, 2014

According to industry experts in case of new market opportunities the local companies are able to expand rapidly by several times with the existing labor force. However, Armenia is in strong competition by other countries in EEU. All EEU members are big exporters of ICT services. As of 2014 Belarus exported 1.6 bln USD, Kazakhstan – 0.6 bln USD, Kyrgyz Rep. 0.3 bln USD and Russia 21.2 bln USD ICT services. Russia and Belarus are quite big IT outsourcing markets by themselves. In this context, Armenia's strategy should be:

- Focusing on product development rather than outsourcing,
- Actively take part in the startup industries of EEU countries, become a part of the technology cluster,

- Building close ties with technology sector financing sources,
- Consider technology and knowledge transfer opportunities from other EEU countries,
- Consider leading initiatives in setting up single e-government systems.



3.3.3. State procurement domain

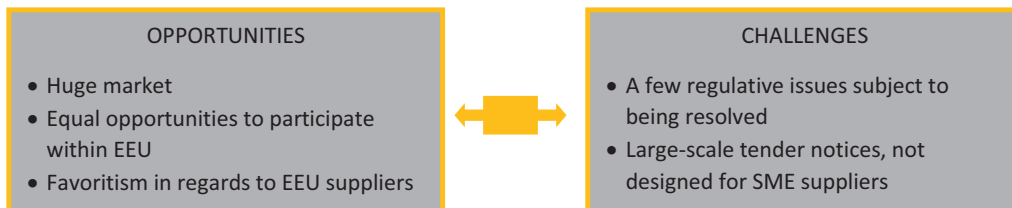
The open access to the state procurement sectors of EEU countries is one of the huge opportunities of this economic integration. As part of Eurasian Economic Union Armenian suppliers have equal opportunities to participate in state procurement tenders and notices. Besides from having equal opportunities, producers from EEU countries have favored conditions –producers from EEU will favor 15% price difference compared to international suppliers (given all other conditions are equal).

In addition, the EEU economic policy has significant level of protectionism and is targeted to be extensively beneficial for its own producers. Thus, the Government of RF has been long discussing the possibilities to significantly limit the products and services of international origin at Russia's state procurement domain. Just recently the Russian Government announced international suppliers of medicaments (over 100 items) applying for state tender notices in Russia should be refused in case there are at least 2 offers from producers from EEU.

According to RF Ministry of Economic Development only the Russian state procured 666.4 bln USD goods and services, 48% of which was spent on the acquisition of construction works and services. Despite the huge state procurement of EEU and immense attractive opportunities there are some challenges and issues to be addressed before the local producers can enter the market. The first and foremost issue as of now is regarding the electronic signatures, due to which Armenian producers are not able to participate in electronic procurement of other EEU countries. RA State Commission for the Protection of Economic Competition announced that it is currently in negotiations with EEU officials to resolve the issue.

In addition, often state procurement tenders have the requirement of the supplier to have at least 3 years of experience in the particular market to be eligible to participate in the call for procurement of products or services.

The high level of corruption in the sphere of state procurement is another impediment for Armenian SMEs to consider entering this market.



3.4. Strategic Horizon 3

The most important strategic opportunities which are expected to drive the economy’s long-term growth and sophistication are categorized in Strategic Horizon 3. The activities are associated with longer-term outlook, regarding the results rather than the required actions and inputs.

The opportunities described in Strategic Horizons 1 and 2 are expected to build the grounds to accommodate more sophisticated economic development stage in Strategic Horizon 3.

The two main tracks of development in this horizon are:

- Armenia, as an economic bridge to EEU;
- Armenia, as a “back office” for EEU business activities.

Premises for successful strategy in Horizon 3

- Renewed relationships with EU

On December 7 Armenia and EU commenced a new round of negotiations. Continuing the negotiations, after Armenia refused to sign the Association agreement with EU, is considered as an unexpected and very “soft” politics towards Armenia. According to the opinions of political experts Armenia has an exclusive chance to negotiate favorable terms for this new potential partnership. The new document which will replace the EU-Armenia Partnership and Cooperation Agreement (1999) will be designed to include Armenia’s new obligations regarding to its membership in EEU.

In case Armenian diplomacy is successful in designing and negotiating economically and politically efficient terms, which is quite plausible and doable in the current conditions, Armenia can favor as EU’s partner on special terms within EEU and can have a role in 2-way EU-EEU relationship.

- Strong interest in partnership by Iran

Having severe political and economic sanctions applied by world leading countries, the interest of Iran in Armenia has increased significantly. The main domains of partnership have so far been several large-scale ongoing or potential projects in infrastructure, and especially energy sectors. In addition, Iran has been one of the biggest trade partners for Armenia especially by agricultural products. By Armenia’s entry into EEU discussions on expansion of cooperation framework have been intensified. Negotiations on possible partnership have been led both on the levels of state officials and business representatives. The role of Armenia as a “gate to markets” can be two-way: EU and EEU trading in huge Iranian market; and Iran trading in EEU market. Iran has numerously announced about its significant interest and intentions and expanding business activities in EEU.

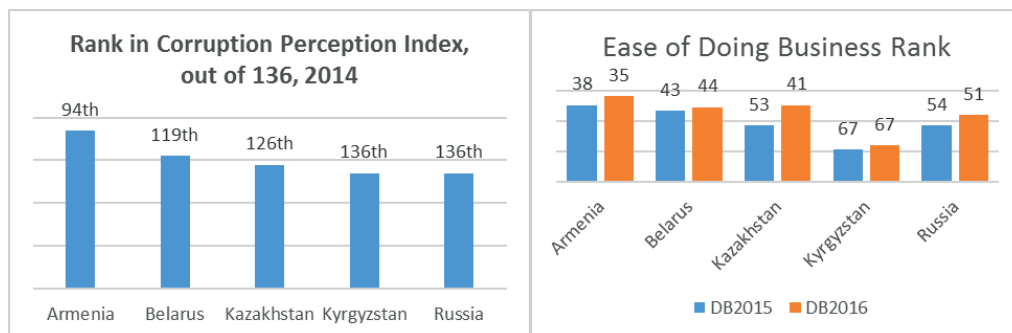
Several sectors are of special highlight in this prospect: the industry of construction materials, chemical products, agricultural products and telecom.

Possible formats of partnership include but are not limited to joint ventures with Iranian companies setting up the final phases of their production chains in Armenia, re-exporting and setting up sales offices in Armenia.

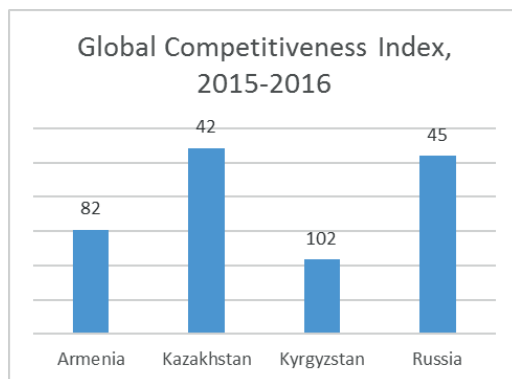
The potential of strengthened economic ties with Iran is momentous for Armenia. It is vital to be quick in setting up necessary infrastructure, such as free trade zones with Iran, for cooperation to take place.

- Comparably higher level of institutional development

As a potential business partner, Armenia has numerous competitive advantages against other EEU members, one of the most important of which is quite impressive accomplishments in institutional domain compared to EEU countries. Among those Armenia stands out with better positions in corruption perception, as well as doing business domains.



Source: Transparency International, The World Bank



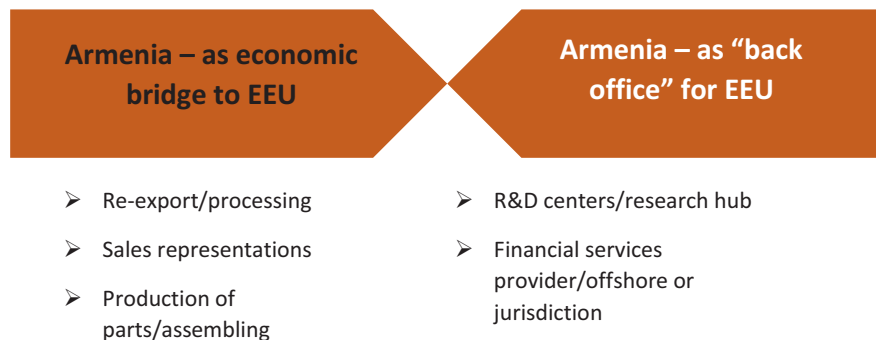
Source: World Economic Forum

Global Competitiveness Index, 2015-2016, by sub-indices

	Armenia	Kazakhstan	Kyrgyz Republic	Russian Federation
1st pillar: Institutions	76	50	115	100
2nd pillar: Infrastructure	82	58	114	35
3rd pillar: Macroeconomic environment	72	25	80	40
4th pillar: Health and primary education	95	93	98	56
5th pillar: Higher education and training	72	60	80	38
6th pillar: Goods market efficiency	50	49	81	92
7th pillar: Labor market efficiency	58	18	88	50
8th pillar: Financial market development	94	91	102	95
9th pillar: Technological readiness	75	61	95	60
10th pillar: Market size	116	46	118	6
11th pillar: Business sophistication	97	79	118	80
12th pillar: Innovation	107	72	125	68

Source: World Economic Forum

As analysed, the opportunity for Armenia to become the “entry gate” to EEU is quite appealing. The main formats of becoming such a bridge and easing the access of third countries into EEU, can be:



The presented strategic horizons are possible scenarios and opportunities for Armenia’s development within EEU. However, these are not default options just given to the country. The membership in the economic union can have a reverse effect, if the economy fails to quickly setup necessary infrastructure to absorb the current opportunities or if the policy makers fail to predict and mitigate risks and challenges for the country in this new economic reality.

CHAPTER 4. RECOMMENDATIONS FOR A WIDER ENTRY OF A SINGLE MARKET

The present exercise aims to show a pattern of how the integration processes into an entity that offers a wider market and resources affect the development of a country. The belief is that the important point of the integration is not only which country integrates where but how the integration is managed. The study aims to claim that the Eurasian Economic Union (EEU) integration, if managed well, can be successful for the countries that make it up, the same way as the EU integration was successful and for the Baltic States and the Eastern European states.

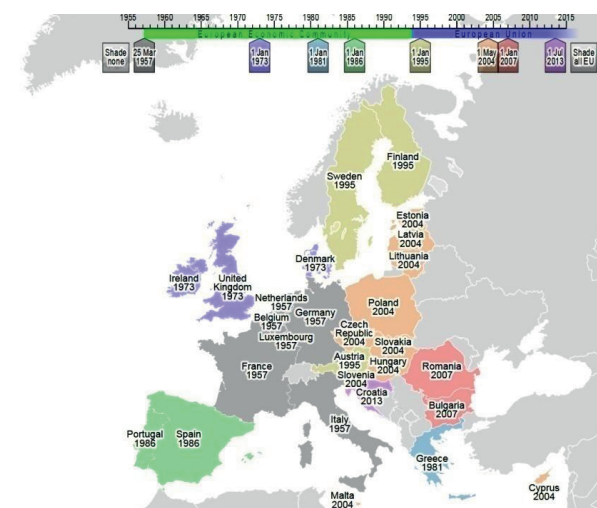
The EU Enlargement and the EU single Market

The 2004 enlargement of the European Union was the largest single expansion of the European Union (EU), in terms of territory, number of states, and population to date; however, it was not the largest in terms of gross domestic product. It occurred on 1 May 2004.

The simultaneous accessions concerned the following countries, sometimes referred to as the "A10" countries:

Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia. Seven of these were part of the former Eastern Bloc (of which three were from the former Soviet Union and four were members of the Visegrad Group), one of the former Yugoslavia (together sometimes referred to as the "A8" countries), and the remaining two were Mediterranean islands and former British colonies.

Part of the same wave of enlargement was the accession of Bulgaria and Romania in 2007, who were unable to join in 2004, but, according to the Commission, constitute part of the fifth enlargement.



For our purposes we will study the journey of three Baltic States (former USSR states), three Eastern European countries and one Balkan country as they went to become members of the EU in 2004 and up to now.

The mere analysis of GDP per capita (USD) of all 7 countries shows the following pattern:

Countries	2004	2014	Growth (%)
Estonia	14628	26902	83.37
Latvia	12505	22823	82.51
Lithuania	13255	26746	101.78
Hungary	16466	24709	50.06
Czech Republic	20970	30366	44.80
Poland	13054	24430	87.14
Slovenia	22693	29969	32.06

Data Source: OECD

Every single country in this list registered in between 32 and 101 per cent GDP growth per capita during the last 10 years, a significant growth due to the new economic environment that these countries found themselves into.

This is due to the philosophy of the Single Market that refers as one territory without any internal borders or other regulatory obstacles to the free movement of goods and services. A functioning Single Market stimulates competition and trade, improves efficiency, raises quality, and helps cut prices. It instigates economic growth and makes the everyday life of businesses and consumers easier.

These countries benefited from the concept of Single Market for Goods and Services that in general offers:

For businesses:

- a 'home market' of over 500 million consumers for their products
- easier access to a wide range of suppliers and consumers
- lower unit costs
- greater commercial opportunities
- freedom to establish a company in another country
- freedom to provide or receive services in another country other than the one where the company or consumer is established.

For Citizens:

- competitive prices
- more innovation and faster technological development
- higher standards of safety and environmental protection.

To add to all this, is the free movement of workers and capital.

One single difference so far is the absence of a major single currency in the EEU against presence of Euro. However, even in this case the similar pattern exists in terms of such a major country as the UK being a member of a the EU and EU single market, while still operating its own currency, the Pound.

Eurasian Economic Union

In its nutshell, all the components above are, too, present in the Eurasian Economic Union. So one couldn't help assuming that the overall process of formation and development of the Eurasian Economic Union in its very essence is similar to what the European Union went through, and the mechanisms and the driving forces of the EEU economy and market are in essence not too much different from those of the EU.

The Eurasian Economic Union is an international organization for regional economic integration. It has international legal personality and is established by the Treaty on the Eurasian Economic Union.

The EEU provides for free movement of goods, services, capital and labor, pursues coordinated, harmonized and single policy in the sectors determined by the Treaty and international agreements within the Union.

The Member-States of the Eurasian Economic Union, Republic of Armenia, the Republic of Belarus, the Republic of Kazakhstan, the Kyrgyz Republic and the Russian Federation, jointly have a population of 182.1 million, cover an area of 20 mln sq.km The total annual GDP of the Union is USD 2.2tn (3.2% of the world GDP), industrial production is USD 1.3 tln (3.7% of the global industrial production), external trade of USD 877.6bln (3.7% of the world export and 2.3% of the world import).

The Union is being created on the philosophy to comprehensively upgrade, raise the competitiveness of and cooperation between the national economies, and to promote stable development in order to raise the living standards of the nations of the Member-States.

Keeping in mind that the aim of this exercise is not to compare the advantages of one block vis-a-vis the other but to seek and offer the new opportunities that the membership to the EEU may provide to Armenia, one could argue that if skilfully explored and managed, a membership to a large economic block, such as the factual case of Armenia becoming a member of the EEU since January 2015 could provide with massive opportunity for a small country like Armenia is, exactly the same way as Baltic, Eastern Europe and Balkan countries benefited from their membership to the European Union.



Source: Eurasian Economic Commission

One thing that we should mind and make no mistake about, is that the benefits and advantages are not coming and will not come automatically and as granted. To make the best out of membership to the EEU, Armenia and Armenian business have to work hard and long to materialize the benefits that the membership to the EEU POTENTIALLY offers.

To make a case how universal the pattern is for Armenian business to make its way to the EEU as its own Single Market and for a British company to make its way to the EU as its own respective Single Market entity, we would bring a number of case studies that the British Government Trade and Investment Department offers on its official web-page as an example of a success story to penetrate a fellow Single Market.

Here are their tips.

- “do lots of research and choose your target regions carefully”
- “spend time in the region asking partners and retailers what they would like to see from you”
- “adapt your product range for each country”
- “hire a high quality local manager who is prepared to work as a lone wolf at the start”
- “be prepared for the long haul - it won’t happen overnight”
- “keep local support staff fully briefed on what the objectives are and how things are progressing”
- “maintain motivation”

The company turnover has increased by 20% in a particular year as the business introduced new product lines and expanded further into its own Single Market. Sales growth was 50%.

Tips from another successful company go as follows:

- “tailor your marketing as your customer base won’t necessarily be the same across the [Market] - always be prepared to adapt your approach”
- “never just assume if you can sell your product in one member state that you can automatically in another - while regulations are harmonized, you still find specific requirements in some member states”
- “always have a local presence, but make sure you get your local representative to spend time with the [original] part of the business so they understand and believe the culture of the business here”
- Understand each market’s needs
- Stay close to your markets
- Get the right stockholding
- Take a close look at country-specific regulations

If we transfer the tips that British companies are providing to their fellow partners towards expanding into the EU Single Market, exactly the same tips are absolutely relevant to the Armenian companies that are looking to expand into the Russian, Kazakh, Belarus and Kirgiz markets, that's how similar the set up is.

The whole point is whether the potential will be possible for companies to materialize into a practical benefit. Here it depends on the companies’ hard work and dedication as well as on the state agencies in Armenia and Armenian representations in other EEU countries to support the companies with vital country-specific advice and export-facilitation support.

In the next section we will have a closer look at what specific recommendations on entrance into the “niche” markets in Russia, Kazakhstan, Belarus and Kyrgyzstan.

Recommendations on entrance into the identified “niche” markets within EEU

For the purposes of the current research the recommendations on entrance into the identified “niche” markets within EEU will be divided into three dimensions:

- State Agency-Level Recommendations for Armenian Government
- Business Union Agency-Level Recommendations
- Individual Business- Level Recommendations

State Agency-Level Recommendations aimed at the Armenian Government and Business Union Agency-Level Recommendations aimed at Business Unions of Armenia are universal and applicable on entrance to all EEU countries and will be discussed before proceeding to individual country recommendations at Individual Business-level recommendations to Armenian business unions and business entities.

State Agency-Level Recommendations

When making appropriate recommendations the line of this research is the same as already indicated earlier above, i.e., the belief is that the important point of the integration is not only which country integrates where, but how the integration is managed and that the Eurasian Economic Union (EEU) integration, if managed well, can be successful for the countries that make it up, the same way as the EU

integration was successful for the Baltic states and the Eastern European states. Exactly the same way, the recommendations envisaged in this paper on entrance into the identified “niche” markets within EEU are not limited to exclusively to how to enter the “niche” markets within EEU but could be with the same success applied to enter “niche” markets of the EU and other unions and individual countries.

Armenian Government Export Promotion Body

One of the most important steps towards promoting export to the EEU should be the encouraging role of the Government of Armenia towards facilitating the exports of Armenian companies to the EEU through establishment and operations of Armenian Government Export Promotion Body. The aim of the body will be to direct the mainstream of export via permanent information feed and linking Armenian business unions and individual businesses with the opportunities in the EEU countries in particular, and other countries in general. The body shall also hold permanent contacts with business unions and individual businesses to receive their feedback on the export process experienced by the businesses and addressing the issues that businesses may raise as experienced by them and which will be within the domain of a state to address, such as legislation irregularities, artificial barriers caused by third-country state agencies, etc.

Among other activities the body would engage into would be promoting awareness raising around Armenian brands as well as facilitating B2B contacts, such as through:

- encouragement of international business forums in Armenia;
- preparation of corresponding product/service catalogues which will represent Armenian products and services;
- participation in investment road shows with a brand "Made in Armenia";

Strengthening the Institute of Trade Representatives (Attachés) of Armenia in the EEU states

It is imperative that while integrating into the EUEU Armenia strengthens its positions on ground in each of the EEU countries through establishing where absent and strengthening where already available, the institute of the Trade Representative of Armenia under the auspices of the Armenian Embassies in the EEU countries. The trade representative shall be responsible for developing and coordinating Armenian international trade, commodity, and direct investment policy in the country under the overall supervision by the Ambassador, and shall oversee the trade relations with a country of duty. The representative shall:

- Provide key day-to-day economic (macro and micro) data and analytics to the Armenian Embassy in the country and back to the colleagues in the relevant government ministries of the Government of Armenia, prepare regular reports and briefing notes on the state of business and trade , and the country in general;
- Build up commercial support function of the Armenian Embassy in the country of residence and support re-establishing the Embassy economic perspective;

- Provide regular analysis and flag-up the business opportunities for Armenia in the country of residence;
- Directly engage with local businesses, business unions and state agencies to ensure to deliver the opportunities to the Armenian businesses and to facilitate doing business for Armenian companies on the specific country of residence.

Armenia should have a full-time Trade Representative in every EEU country irrespective of the fact if Armenia has a physical presence in the form of an Embassy in that country.

Business Union (Association) Agency-Level Recommendations

The major role of business unions (associations), including sectoral, is collective action to protect common interest. Collective action is defined by the World Bank as “a collaborative and sustained process of cooperation between stakeholders.” The practice shows that collective action increases the impact and credibility of individual action, individual players into an alliance of link-minded organizations and levels the playing field between competitors. It is a strategic approach where businesses, unified around common aims, work together as part of their short or long term export strategy development. Collective action approaches tend to be more successful when supported by a facilitator. Potential facilitators include chambers of commerce, business associations, or trade unions, among others. In this light it is very important for the Armenian sectoral business unions (associations) to play a coordinating and facilitating role in between linking the opportunities in the EEU countries to the businesses within the respective sector, strengthen the whole business sector and create an opportunity every business entity in that sector interested in exporting. The actions that business unions (associations) should take in this regard include but are not limited to the following:

- Establishing and keeping close links with appropriate business unions (associations) in Belarus, Kazakhstan, Kyrgyzstan and Russia with a view of obtaining relevant useful information and passing it on to the member business entities in Armenia.
- Establishing and keeping close links with the Ministry of Economy of Armenia, Ministry of Foreign Affairs of Armenia, Ministry of International Economic Integration and Reforms, Armenian embassies in the EEU countries with a view of obtaining relevant useful information and passing it on to the member business entities in Armenia, as well as channelling any feedback obtained from the sectoral businesses in the exporting process that may be relevant for all those entities to address.
- Support develop and implement by the member sectoral businesses common action that will strengthen their position and enhance their chances of exporting their products and services such as advising on standards and export regulations required by this or that country or sharing best/local practice experience as suggested by fellow chambers (associations) in the appropriate countries.

Chambers of commerce, unions and associations, as a form of business network, whose goal is to further the interests of businesses shall directly implement its functions. This is not the same as doing business for/instead of businesses as such. It is important to always keep in mind that it is the sole responsibility of the business to follow-up with making its business conducts a success. It is important to realize that the sectoral unions are playing a supporting and facilitating role only and are not a substitute to which doing business can be outsourced.

Individual Business- Level Recommendations

Kazakhstan

The population of Kazakhstan is approximately 17 million, with approximately 1.8 million living in Almaty, the largest city, and a further 732,000 in Astana, the second largest city. With GDP per capita of over USD 12000 it represents a potential vast market for Armenia within a Single Eurasian Economic Union market. Whereas the actual figures show that there virtually no trade between Kazakhstan and Armenia.

In 2014 Armenia exported to Kazakhstan good and services of the value of less than USD 7 mln, or less than 0.4% of the total exports to the EEU. And within 7 months of the 2015 exports to Kazakhstan accumulated a mere USD 3.6mln.

2014: Armenia's Trade with Kazakhstan (USD, mln)

Source: National Statistical Service of the Republic of Armenia

Year	2014 EEU	% of total	of which	Kazakhstan	% of total
Export	324238.5	20.9		6951.8	0.4
Import	1154463.8	26.0		556.3	0.01
Total	1478702.3	24.7		7508.1	0.1

2015: Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)

Source: National Statistical Service of the Republic of Armenia

Year	2015 EEU	% of total	of which	Kazakhstan	% of total
Export	236246.5	15.9		4857.7	0.3
Import	982124.6	30.1		292.4	0.009
Total	1218371.1	25.7		5150.1	0.1

The conclusion is that Kazakhstan represents an underexplored, underused and undervalued market for Armenian exporters, which stands as below:

Main export items in Armenia's export portfolio, 2014

Commodity groups	Share in Armenia's exports, 2014	Exports value, USD, 2014
Mineral products	26.1%	389,383,148
Base metals	20.3%	302,300,014
Alcoholic beverages	11.9%	177,011,237
Diamonds	7.9%	118,017,982
Tobacco	7.8%	115,881,754
Precious or semi-precious stones, precious metals	5.9%	88,241,739
Machinery, products of engineering	3.4%	50,166,363
Textiles	3.3%	49,899,316
Fish and aquatic products	2.0%	30,516,949
Vegetables and fruits	1.7%	25,797,804
Jewellery	1.5%	21,739,954
Articles of stone, plaster, glass, etc.	1.4%	21,030,074

Kazakhstan is a large importer country with imports of around USD 50bln a year, of which a range of products that make up part of Armenia's export structure, such as:

Vegetables and fruits- USD 1.21bln, of which:

apricots-USD 52mln,

grapes-USD 36mln

Animal Products- USD 865 mln, of which:

cheese - USD 65 mln

Foodstuff- 2.21bln, of which:

chocolate- USD 256 mln,

fruit juice- USD 65 mln,

rolled tobacco- USD 136 mln,

hard liquor- USD 132 mln,

wine- USD 50 mln,

processed fruits- USD 60 mln,

processed tomatoes- USD 21 mln,

Shoes- - USD 613mln

Textile- - USD 1.71bln

Market entry recommendations

A number of tips that an Armenian company should apply in Kazakhstan are universal tips that are applicable to every country and which are summarized in the case studies that the British Government Trade and Investment Department offers on its official web-page as an example of a success story to penetrate a fellow Single Market for the British businesses:

- “do lots of research and choose your target regions carefully”
- “spend time in the region asking partners and retailers what they would like to see from you”
- “adapt your product range for the country”
- “hire a high quality local manager who is prepared to work as a lone wolf at the start”
- “be prepared for the long haul - it won’t happen overnight”
- “keep local support staff fully briefed on what the objectives are and how things are progressing”
- “maintain motivation”

As mentioned earlier in the work, all these tips are universally applicable for Armenian businesses to enter the EEU market, including Kazakhstan.

Kazakhstan offers many opportunities, but they may not be the right market for all firms. According to U.S. Department of Commerce’s International Trade Administration export facilitation wing, the companies that meet one or more of the following criteria will have an edge:

Export sales and emerging markets are an important part of the company business;
 The firm has experience in Eastern Europe, the Caucasus, Russia, or Ukraine;
 The company is willing to invest into time, effort, and resources for the long term.

Most exporters find using local distributors an easy first step for entering the Kazakhstani market. A local distributor is typically responsible for handling customs clearance, dealing with established wholesalers/retailers, marketing the product directly to major corporations or the government, and handling after-sales service, if required. It is not uncommon to partner with a firm that is involved in several unrelated sectors. Other useful early steps include:

- Performing detailed market research to identify specific sector opportunities.
- Establishing a local presence or selecting a local partner for effective marketing and sales distribution in Kazakhstan. Keep in mind that Kazakhstan has a population spread over a large landmass, and distribution channels should be able to represent the company needs countrywide. Due diligence is also a must.
- Maintaining a long-term timeframe to implement plans and achieve positive results. Don’t expect this to be an inexpensive market that can be entered quickly.
- Be prepared to assist your buyers to obtain financing (see Chapter 7.)

UK Trade and Industry recommends considering the following as main routes to Kazakhstan market:

- setting up a Joint Venture (JV) with local partner
- exporting via a local agent or distributor
- setting up a local company

Helpful contacts for foreign in Kazakhstan

The Ministry for Investment and Development of the Republic of Kazakhstan is one contact point to obtain more information on the business opportunities in Kazakhstan.

Ministry of National Economy of the Republic of Kazakhstan is another contact point to obtain more information on the business opportunities in Kazakhstan.

The National Chamber of Entrepreneurs of the Republic of Kazakhstan is the non-governmental business contact point for those aiming at doing business with/in Kazakhstan.

Belarus

The population of Belarus is approximately 10 million, and a GDP per capita of over USD 8000 Belarus represents another potential vast market for Armenia within a Single Eurasian Economic Union market. However, the figures show little export trade between Armenia and Belarus.

In 2014 Armenia exported Belarus goods and services of the value of a mere USD 9 mln, or less than 0.6% of the total exports to the EEU. And within 7 months of the 2015 exports to Belarus accumulated a mere USD 3.2mln.

2014: Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)
Source: National Statistical Service of the Republic of Armenia

Year	2014 EEU	% of total	of which	Belarus	% of total
Export	324238.5	20.9		9036.5	0.6
Import	1154463.8	26.0		31031.5	0.7
Total	1478702.3	24.7		40068.0	0.7

2015 Armenia's Trade with the Countries of Eurasian Economic Union (USD, mln)
Source: National Statistical Service of the Republic of Armenia

Year	2015 EEU	% of total	of which	Belarus	% of total
Export	236246.5	15.9		5461.8	0.4
Import	982124.6	30.1		33787.6	1.04
Total	1218371.1	25.7		39249.4	0.8

As with Kazakhstan the conclusion is that Belarus represents an underexplored, underused and undervalued market for Armenian exporters.

Belarus mainly imports energy resources (oil and natural gas), raw materials and components (metals and metal products, raw materials for chemical industry, machine parts) manufacturing equipment.

Today Belarus has trade relations with more than 180 countries around the world.

Russian Federation is the major trade partner of the Republic of Belarus, it accounts for more than 40 percent of export and more than a half of volume of import.

The European Union is the second largest trade partner of the Republic of Belarus, it accounts more than 30 percent of export and one fifth of import. The main partner in the EU are Great Britain, Netherlands, Germany, Lithuania, Italy, Poland, Latvia, Belgium, Czech Republic.

The major foreign trade partners of Belarus within the CIS are Russia, Ukraine and Kazakhstan.

There is a positive dynamic in cooperation with the traditional partners in Latin America such as Brazil, Venezuela and Ecuador, and in Asia, notably with China, India, Indonesia and Turkey.

Of imports of around USD 45bln a year, a range of products make up part of Armenia's export structure, such as:

Vegetables and fruits- USD 1bln, of which:
apricots-USD 4mln,
grapes-USD 45mln

Foodstuff- 1.91bln, of which:
chocolate-USD 140mln,
hard liqueur- USD 65mln
fruit juice- USD 37mln,
rolled tobacco and cigarettes - USD 130mln,
beer- USD 84 mln,
wine- USD 75mln,

Shoes- - USD 297mln

Textile- - USD 960mln

Market entry recommendations

Government official etiquette – quick tips

The government in Belarus is working to make state organizations more accessible to foreign partners and investors.

A meeting with a Belarus state official will be more official than with businessmen.

The level of manager you meet will depend on the status of your own organisation. If the meeting is going well, it's common for more senior managers to be brought in.

Business etiquette – quick tips

- Business meetings tend to be low key but formal, so dress smartly.
- Personal relationships are very important – establishing a partnership based on trust is essential to doing business successfully.
- Be patient. If you have a good product and a fair price you are likely to succeed, though the process may take longer than in other countries.
- Older people in Belarus will introduce themselves using their first name and patronymic (the name from their father) and you should use this when addressing them.
- Before you travel to Belarus get some business cards printed with English on one side and Russian on the other. Give these out to everyone in the room at the start of the meeting.
- Employ a good local interpreter.
- It's considered poor form to criticize the host country.
- Have an open mind to try any food or drink offered to you.
- Don't adopt an overly rigid approach to prices and agreements: be prepared to negotiate and make concessions.

Foreign investment in Belarus increased 13-fold in 2002-2010 while the volume of foreign trade quadrupled. In 2014 foreign investors poured \$15.1 billion into the real sector of the Belarusian economy.

If you want to trade as a foreign or international company in Belarus, you need to set up in one of two ways:
as a representative office (RO) or as a legal entity.

Both options require you to register with the Tax Authorities.

Traditionally representative offices in Belarus were just that – organizations operating as ambassadors for foreign companies, but without a taxable presence in the country. Today you can have a taxable presence with a RO, and can sign contracts and carry out negotiations. However, if you want to carry out long-term commercial activity within Belarus, setting up a legal entity may be a better option. Belarusian laws provide for various organizational-legal forms of commercial organizations.

Most legal entities choose the following types as the most convenient for business:

Joint Stock Companies

Limited Liability Companies

Unitary Enterprises

A number of tips that an Armenia company should apply in Belarus are universal tips that are applicable to every country and which are summarized in the case studies that the British Government Trade and Investment Department offers on its official web-page as an example of a success story to penetrate a fellow Single Market for the British businesses:

“do lots of research and choose your target regions carefully”

“spend time in the region asking partners and retailers what they would like to see from you”

“adapt your product range for the country”

“hire a high quality local manager who is prepared to work as a lone wolf at the start”
“be prepared for the long haul - it won’t happen overnight”
“keep local support staff fully briefed on what the objectives are and how things are progressing”
“maintain motivation”

As mentioned earlier in the work, all these tips are universally applicable for Armenian businesses to enter the EEU market, including Belarus.

Helpful contacts for foreign businesses in Belarus

The National Agency of Investment and Privatization

The National Agency of Investment and Privatization was set up to attract inward investment and help international companies in Belarus.

Services for foreign investors in Belarus include:

- preparing investment proposals
- looking for potential investors
- research and analysis for potential investors
- facilitating interaction with Government bodies and national institutions
- arranging meetings with Government officials and others
- introductions between Belarus businesses and foreign partners
- newsletters and market research
- support and guidance

Belarusian Chamber of Commerce and Industry

The Belarusian Chamber of Commerce and Industry is one of the main public organisations representing international trade in Belarus.

This organisation helps with many aspects of business in Belarus, including:

- finding business partners for foreign businesses
- help for Belarusian companies trading abroad
- legal and commercial advice
- translation and interpreting

Belarusian Universal Commodity Exchange

Belarusian Universal Commodity Exchange (BUCE) is the only mercantile exchange in the Republic of Belarus and one of the largest spot exchanges in Eastern Europe. BUCE’s main function is assisting Belarusian companies with sales of their products in foreign markets and helping foreign companies to access the Belarusian market.

BUCE has branches in all the regional centers of the Republic of Belarus.

Ministry of Economy

The Ministry of Economy is the Government Ministry responsible for fostering economic ties with other countries and developing the economy of Belarus.

Kyrgyzstan

The population of Kyrgyzstan is approximately 6 million, and a GDP per capita of over USD 1270. Kyrgyzstan represents a small but still a potential market for Armenia within a Single Eurasian Economic Union market.

However, the figures show almost no export trade between Armenia and Kyrgyzstan in 2014, a mere USD 0.37mln of export. The trend is the same for 2015.

Of imports of around USD 7bln a year, a range of products make up part of Armenia's export structure, such as:

- Vegetables and fruits- USD 200mln, of which:
 - grapes-USD 1.3mln
 - foodstuff- USD 440mln, of which:
 - chocolate-USD 69mln,
 - hard liqueur- USD 17.5mln
 - fruit juice- USD 4.8mln,
 - rolled tobacco and cigarettes- USD 66mln,
 - beer- USD 13 mln,
 - wine- USD 4.8mln.
- Shoes- - USD 130mln
- Textile- - USD 1.36bln

Market entry recommendations

Establishing a business

Resolved forms of creation of enterprises

In order to start an activity in territory of the country, the legal entity should be registered in three state bodies: Ministry of Justice of the Kyrgyz Republic (there are a regional representative offices in each oblast of the country), National Statistics Committee which enters registration data into United Single State Register of Statistics, and State Tax Inspectorate (STI). Individual businessmen should register only in statistical committee and in Tax Inspectorate.

Foreign investors have the same legal status as Kyrgyz investors and can implement activities as a complete foreign enterprise or in partnership with Kyrgyz or foreign entrepreneurs. Foreigners can buy stocks and other securities of Kyrgyz companies and participate in privatization programmes.

Registration procedures

In order to register in the Ministry of Justice of the Kyrgyz Republic, a representative of the company or the founder should present following documents:

- An application for registration;
- Other documents depending on the form of the company;

If one of the founders is a foreign legal entity, in order to register it is necessary to give the legalized extract from the registrar, certifying, that the founder is a legal entity in accordance with the legislation of his/her country.

In order to register a joint-stock company, the founder should give a letter from the bank confirming submission of 50 % of the authorized capital.

A foreign citizen who is acting as the founder should additionally present copy of his/her passport or any other identification document (with duration of visa).

All documents should be accompanied by notary certified translation to Kyrgyz or Russian.

Registration of enterprises in Free Economic Zones

There is a special procedure for registration of the enterprise in the Free Economic Zone (FEZ). Enterprises should be registered in management of FEZ.

Registration of the individual entrepreneurs

The National Statistical Committee and its departments in regions register individual entrepreneurs depending on their location. Registration is carried out on the basis of the registration application and the passport. After registration Statistical body gives a registration certificate with individual identification number.

Registration of branches and representations

Registration of branches and representations is carried out the same as registration of legal entities. There is a requirement about presenting additional documents: regulations about branch or representation and copies of the registered documents of the person, organizing the branch or representation. A foreign enterprise or a physical entity should also present an extract from the trading registrar system or other document confirming, that the company, organizing branch/representation in the Kyrgyz Republic, is a legal entity in accordance with the legislation of the country and a letter from the bank confirming his/her solvency. All documents should be accompanied by notarial- certified translation into Kyrgyz or Russian languages.

Overview of Foreign Investment Climate

The Kyrgyz Republic has a liberal investment regime on paper with a broad base of commercial laws in place. These laws, however, are not always implemented consistently and the legal concept of contract sanctity is problematic.

The Kyrgyz Republic is open to foreign direct investment and the government publically recognizes that foreign direct investment is an important component to growing the economy.

Laws exist that make the investment climate more favourable, than previously, for foreign companies.

Foreign exchange is widely available and competitive.

The Law on Commercial Arbitration allows for international and domestic arbitration of disputes.

The Kyrgyz Republic is a member of the International Center for the Settlement of Investment Disputes (ICSID). It signed the ICSID agreement on June 9, 1995, and ratified it on July 5, 1997. The Kyrgyz Republic became a member of the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards on March 18, 1997.

A World Trade Organization (WTO) member, the Kyrgyz Republic is compliant with WTO Trade Related Investment Measures obligations. The Kyrgyz government also reduced the tax burden on repatriation of profits by foreign investors to conform to the tax rate for domestic investors.

Foreign and domestic private entities may own business enterprises and engage in a broad range of commercial activities. Foreign entities are expressly forbidden from owning land, including farmland, although regulations allow for up to 99-year leases of property.

There is no prohibition on foreign rental of land for residences or factory sites. A central land registry has helped potential lenders and others deal with the financing of real property (e.g., land, buildings, and other improvements). Yet, the banking system of the Kyrgyz Republic remains relatively undeveloped and uncompetitive by international norms.

Property right protections are slowly emerging.

The Kyrgyz Republic is obligated to protect intellectual property rights as a member of the WTO. The Kyrgyz Republic acceded to both the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty in 2002. Counterfeit goods made primarily in China, however, are widely available.

Helpful contacts for foreign businesses in Kyrgyzstan

There is an investment department at the Ministry of Economy and Antimonopoly Policy, which assists investors with bureaucratic procedures. This department also consolidates information about potential investment projects in the Kyrgyz Republic. However, the total efficacy of this office in assisting firms

with setting up shop is limited since official bureaucratic procedures comprise only some of the hurdles to opening a business.

An Investment Council, under the auspices of the president, exists to further regulatory improvements for the business climate.

Being a small and a poor market, Armenian business will be facing in Kyrgyzstan the same challenges as any other foreign business targeting the country. One thing Armenian business should do when considering doing business in Kyrgyzstan is considering the volume of effort spent on exploring the market vis-a-vis the expected gain. By far Kyrgyzstan is the most difficult and the least attractive market among all EEU markets.

Russia

The analysis of the country trade structure for Armenia with the EEU countries shows that Armenia's main and largest trade partner within the EEU was and remains the Russian Federation, with around 95% of all Armenia's trade with the EEU countries falling on Russia. Armenia has grown its export to Russia on a year-by-year basis, and so have been the imports from Russia, with an overall trade balancing around USD 1.4-1.5 bln a year.

The structure of Armenia's export to Russia, main categories, in 2014 (source: International Trade Centre)

2014: Armenia's Trade with the Countries of Eurasian Economic Union (mln USD,)
Source: National Statistical Service of the Republic of Armenia

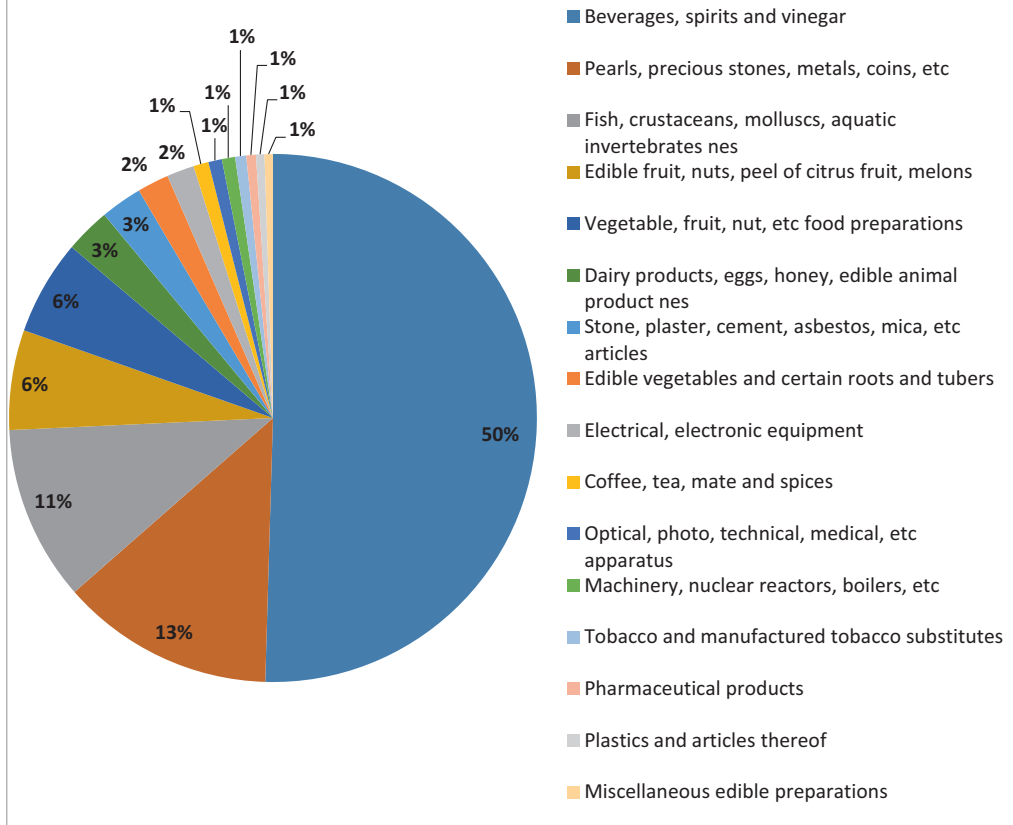
Year	2014 EEU	% of total	of which	Russia	% of total
Export	324238.5	20.9		308250.2	19.9
Import	1154463.8	26		1122876.0	25.3
Total	1478702.3	24.7		1431126.2	23.9

2015: Armenia's Trade with the Countries of Eurasian Economic Union (mln. USD)
Source: National Statistical Service of the Republic of Armenia

Year	2015 EEU	% of total	of which	Russia	% of total
Export	236246.5	15.9		225927.2	15.1
Import	982124.6	30.1		948044.6	39.1
Total	1218371.1	25.7		1173971.8	24.8

Of almost USD 1.5bln of exports, Russia's share of Armenia's export makes up around 320mlnUSD, of which 80% accounts for food and agriculture products, 12% accounts for precious metals, and 3%- on machinery.

Russian Federation's imports from Armenia in 2014, main categories



Source: International Trade Centre

Market entry recommendations

Russia was the world's ninth largest economy by Gross Domestic Product (GDP) in 2014 according to the (IMF).

The main forms of business activity used by companies in Russia are:

- direct sales
- distributorship agreement
- representative offices
- branch of a foreign legal entity
- subsidiary

Representative offices are accredited for 1 to 3 years. They can only carry out activities aimed at generating profit, such as market research. They can use rouble and foreign currency bank accounts and transfer funds without restrictions.

A branch of a foreign legal entity is accredited for 1, 2, 3 or 5 years. They can carry out all the functions of the company in the Russian Federation.

Companies can choose to establish a presence in Russia through a Russian subsidiary. The most common business structures in Russia are:

- limited liability company (OOO in Russian)
- closed joint stock company (ZAO in Russian)
- open joint stock company (OAO in Russian)

A few tips for doing business in Russia

- Expect to commit significant time, personnel, and capital, as developing business in Russia is resource-intensive.
- Conduct market research, to identify opportunities and potential Russian business partners.
- Conduct significant due diligence, to ascertain the reliability of business partners.
- Consult with Armenian companies already in the market
- Communicate regularly with Russian business partners to ensure common understanding of expectations
- Travel frequently to Russia in order to establish and maintain relationships with partners and to understand changing market conditions.
- Maintain a long-term time frame.

Do or do not do

First, make sure your decision to enter the Russian market is well-grounded. Russian opportunities are often counter-weighted with issues you never faced in other markets. The latter could require extra effort and time devoted. Be prepared to that.

Do market research before diving into the market

In many instances, you don't necessarily need a costly in-depth feasibility study to identify demand for your products in Russia. The Russian market is unsaturated in many sectors. Getting the first reaction among your potential consumers might send you a clear signal whether to proceed further.

Find a reliable partner in Russia

Strictly speaking, market entrants don't need a joint venture in the country to launch Russian operations. However, having a partner who is successful or your provider / supplier speeds up the market entry process significantly. The key to successful partnership is in building trust and personal relationships.

Build trust first

The first meeting rule in Russia is to be open, decisive, clear and straightforward with your offer, as well as highly competent in your product/ service area. Once you get to know each other, clearly show what really makes you different.

Personal relations is key to business success

Don't be surprised if you are invited into the family and house. Russians somehow subconsciously tend to screen you at the personal level to answer the question if you are a trusted person to deal with. Once you establish such relationship, it is a common practice that they will likely introduce you to other decision makers and business connections, thus paving the ground for your business success, leads you need, and sales after all. Personal relations always prevail over formal contracts.

Don't underestimate your Russian partner

Throughout the relationship-building process, be respectful to your partner and openly explain your strategy and plans if you want them to help you. Make sure your partner fully understands your actions and rationale behind them before you take your first step. If you stick to this rule, you might be surprised how creative and efficient your partner is with the solutions proposed.

Competitors and networking value

Be friendly with other companies operating in your chosen area and consider them as your allies rather than your local competitors. That would broaden your business relationships significantly and you'll learn the local landscape much faster.

Stay politically correct

Russians are generally proud of their culture, heritage, and history. Quite often, they appear to be self-criticizing and over-demanding to their political elite. But they don't like outsiders to judge them – Russians believe the internal issues are strictly 'their family business'. So, be focused on business and stay away from criticizing their leaders, politics, and/or traditions. Don't let your unwanted message affect your relationships and, after all, business.

Choose your starting base

It is easier and less costly to start from one geographical location and keep building success from there. That might be a Special Economic Zone (SEZ) that meets your requirements. Another option is your Russian partner's location where your partner is well established and can easily help your new venture to grow fast. Many entrants traditionally choose Moscow or St Petersburg as their entry point, i.e., two major business centres where most of required resources are at arm's reach. There is also a tendency among technology and manufacturing companies to start in a region with existing local facilities and cheaper workforce.

Have professional expertise handy

Cross-border trade is regulated by ever-evolving Russian legal system. So, take a closer look at what your local consultant and/or lawyer recommends as to the business model, customs formalities, papers required, contract contents, logistics operations, and communications with government officers, etc. Local experienced advisors are normally pre-requisite for doing trade transactions the right way.

Payments and due diligence

One of most known myths is questionable payment discipline by Russian contractors. Experts admit that in many cases the Russian contractors/ buyers are willing to pay up front even before the goods delivery, once your relationship is established. However, due diligence is always recommended as another pre-requisite step of your first Russian experience. As a matter of fact, local advisors could perform those checks better and faster than their international counterparts due to peculiarities in information access/ collection practices.

Language, communications, and access to the market

Hiring Russian-speaking staff could easily solve the language barrier issue. Dealing through a local agent/ distributor/ representative could be even more efficient solution. JV opportunity with local established business is another efficient model for successful operation on the market. Don't discard local trade and business associations, which could be extremely helpful (access to local market leaders, faster contractor search and negotiations, efficient due diligence and background checks, etc).

Cultivate government relations

Government relations should be taken very seriously as the State authorities are often the most powerful stakeholder in Russia. Showing respect and getting to know is key. In industry clusters/ Special Economic Zones (like Kaluga or Yaroslavl) it is wise to focus on regional and municipal level. Consider local government as your partner, not just as a taxpayer, and you will be rewarded. It is crucial to show that as an investor you are bringing real benefits to the local communities and people who live there.

Identify the Government needs

Russian Government at all three levels – Federal, regional, and municipal/ local – has multiple programmes to fund public-sensitive projects. Check such government tenders or investment programmes if your product/ service could meet some of those.

Be creative and capitalise on challenges

Be pro-active and creative with identifying your niche with fewer, if any, competitors. For example, Russia's vast territory and underdeveloped transportation infrastructure is considered a challenge for trade. At the same time, Russia has the highest internet and mobile phone penetration across Europe. There are a number of new logistics companies on the market that both undertake delivery to any point on the Russian map and collect payments upon delivery. Use those players as your logistics and payment processing contractors and start selling your goods on-line. Ecommerce is one of the boosting industries in Russia these days with great growth prospects for the years to come.

Looking into future: Projection of benefits of EEU membership: WHENs and IFs

Integration projects like the EU and EEU are formed not for a short time but for decades and longer if things develop as planned. That's why when looking into potential benefits of this or that integration it makes sense to look not only on the present realities but also project the potential benefit given the possible changes in the realities and circumstances.

In the case of Armenia we will today briefly consider a number of IFs and WHENs, as part of looking forward into future and if there are certain developments in the world of international affairs that may have a direct impact on the level of benefit that Armenia may extract from membership to the EEU.

Those are:

WHEN Iran international sanctions are fully lifted

If Abkhazian part of the railway linking Georgia and Russia ever opens

If more member-countries join the EEU

Lifting Iran sanctions

The end to international sanctions on Iran is good news for Armenia, according to analysts.

Armenian Foreign Ministry expected this to contribute to strengthening stability and cooperation in the region, among other positive implications.

Beforehand, cross-border trade was constrained by the sanctions rules. Bank transfers and other financial transactions were complicated, so trade was restricted to bartering and private business deals in cash.

Trade with Iran has fallen by 50 or 60 per cent vis-a-vis its potential, according to industry and entrepreneur representatives. They continued that Armenia has been cut off from the Iranian port of Bandar Abbas in the Gulf, as shipping companies refused to deliver goods to an Iranian port and Armenia has been forced to use the Georgian ports of Batumi and Poti for maritime shipping. Armenian business believes that the easing of sanctions would help diversify export routes, turn Armenia into a pivotal transit route, and restore previous volumes of trade.

On their part Iranian diplomat believe that the lifting of international sanctions against Iran will speed up the implementation of its joint energy projects with Armenia.

They assured that the lifting of international sanctions against Iran will have a concrete impact on Armenian-Iranian projects. Projects will primarily concentrate on the planned construction of a new high-voltage transmission line that will enable Armenia to import much more Iranian natural gas and pay for it with electricity supplied to the Islamic Republic.

Both Armenian and Iranian officials have also referred to the sanctions for repeated delays in the \$350 million construction of a major hydroelectric complex on the Armenian-Iranian border and expected hope that the implementation of the hydroelectric project “will most probably accelerate” as a result of the landmark nuclear deal, including attracting investments into the project.

However, these projects will depend on the availability of investors and economic rationale. For example, the railway construction project requires an investment of \$3.2 billion and for it to be implemented, an investor is needed. No serious investors have been found yet, according to the Ambassador.

The analysis shows that for such big projects become a reality they need to be part of a larger network of infrastructure rather than serve the bilateral interests of two countries.

In this sense opening the Abkhazian part of the railway linking Georgia and Armenia could prove vital for making the railway project between Armenia and Iran feasible and attract investment as it will pave a direct railway route in between Iran, Armenia, Georgia, Russia and further.

Opening Abkhazian part of the railway linking Georgia and Russia

Transportation and, in a wider sense, communication security play a critical role in the Armenian national security system given the closed borders with Turkey and Azerbaijan as result of a blockade by those two countries.

On the other hand Armenia is the aggrieved party of the Georgian Russian and Georgian Abkhaz relations, which have seriously complicated the possibility to use the Abkhaz portion of the railway connecting Armenia and Georgia to the Russian railway.

The communicational position of Armenia may be regarded as “deadlock”, since the country fully depends on freight transit via Georgia and Iran.

Opening the railway communication at the Abkhaz section may become a serious basis for better integration of Armenian business into the one of the EEU.

Armenia is connected by railway to Georgia and to its largest port Poti, which provides access for Armenian importers and exporters to the international market.

Resuming the operation of the Abkhaz railway section will directly connect Armenia via Georgia with Russia and other EEU countries. Plus it makes it feasible the construction of an Armenian-Iranian railway link, the transportation of cargo from Iran to Armenia via the new railway, then via Georgia and Abkhazia to the Russian federal railway stations.

Unfortunately, in the present discussion of the Armenian railway construction issues, the focus is on commodity turnover between Armenia and Iran. Due to small volumes of and one-sided (about 80% of the total freight traffic falls on import from Iran to Armenia) Armenian-Iranian commodity turnover, it is often said the railway is unviable, and must not be built. Such a wrong approach fails to consider the fact that nearly all railways presently being constructed worldwide solve the regional rather inter-state issues. The prospects of making Armenia a transit country, and a transportation hub, which open new opportunities for trade with the South Asia and Middle East, keep up to date the development of the EEU as an organization open for changes, which will be in the process of continuous adaptation considering the nature and geography of its expansion, and interests of its new and prospective members. This, in its, turn, must stimulate Armenia to play an active role in the regional affairs pushing and lobbying for solutions that will be a win-win both for Armenia and the countries in the region.

If more member-countries join the EEU

A number of events during 2015 suggest that the EEU is not planning to limit its scope within the geography of the current 5 member-states only.

In October 2015 Israel announced its interest in signing an agreement on the free trade zone with the Eurasian Economic Union (EEU) as soon as possible. State officials on both sides confirmed they believed in a big potential of such an agreement and gave "high priority" to the talks on the free trade zone. And mid-October, the Supreme Eurasian Economic Council adopted a decision that the Eurasian Economic Union would launch talks with Israel on creating the free trade zone.

In October 2015 Russian Industry and Trade Minister Denis Manturov proposed to establish economic coordination between BRICS and the Eurasian Economic Union (EEU) through working on opportunities for reducing barriers between the BRICS and the EEU in order to boost mutual trade, increase investment and new full-scale industrial projects.

Earlier in June India and EEU began to study the feasibility of a free trade zone agreement. The corresponding document was signed between the Ministry of State for Commerce and Industry of India and EEU at St. Petersburg International Economic Forum (SPIEF 2015).

The research team is tasked to carry out research and bring to the Presidents' decision [of the Union countries and India] on beginning the negotiations on the free trade zone agreement. The group was tasked to analyze the dynamics of trade, investment and overall "joint trade policy and integration agendas.

In May 2015, the EEU has signed an agreement on free trade with Vietnam, which was the first agreement on the facilitation of trade regime after the establishment of the union in 2015.

A similar working process is undergoing with Egypt.

The wider implication of this process is that the more the geography of the deals between the EEU and third countries and blocs reaches the wider the market opportunities for the EEU businesses are becoming, including automatically the Armenian businesses.

