



POLICY NOTE OF THE WORKING PAPER 2/02

Is the EU the best trade partner for its neighbors?

January 2013

OBJECTIVE OF RESEARCH

The main goal of this work is to analyze in depth the bilateral trade relationships between the EU and its neighboring countries over the last fifteen years in order to determine whether trade patterns have changed over time. The European Neighbouring Countries are developing countries (middle-to-low income countries) which, thanks to their proximity to European borders, have close relations with the EU and aspire to become a member state- The current association agreements (MED, South Caucasus and all the bilateral agreements) were put in place in order to facilitate the movement of goods and to attract foreign investment in the neighbouring regions.

To achieve the main objective of this work we have explored trade flows between the EU and the ENC's, moving in different ways. We split ENC's into four different sub-regions in order to understand regional performance.

We have taken into account ENC's trade flows from and to emerging economies and the major world partners so as to determine whether Europe is losing its key role and whether its main competitors are gaining market share in the Europe's neighbouring countries. We have considered trade flows for

different types of products so as to gain an insight into the quality of the trade relationship. Lastly we have examined geographical and sectorial concentration in trade flows in order to analyze to what extent ENCs' trade structure is vulnerable to shocks.

SCIENTIFIC METHODS

The descriptive analysis of this paper is meant to produce new stylized facts about the position of the EUs neighbours in the international arena. The analysis is based on a comprehensive dataset of trade flows, which has enabled us to consider separately goods at the industry level depending on their end use. We can distinguish finished and semifinished products and within the first group we can separate out trade of consumers goods from trade of industrial goods. We can therefore shed some light on a number of aspects: how EU neighbours perform differently according to their geographical position; how they compare with other countries belonging to the same income category; how does their specialization structure in the EU differ compared to other markets, with special attention to emerging economies. In the last part of the paper we investigate, at the country level, the most important (in terms of market share) trade destinations and origins and the most important sector. We calculate the Herfindahl index to determine the degree of trade concentration of the neighbouring countries in different markets.

POLICY VALUE-ADDED

The descriptive analysis in this paper reveals how patterns of economic interaction, between EU and its neighboring countries (ENCs), have evolved over the last fifteen years. ENCs never played a key role in European trade either as a destination or origin country, but recent developments during the last globalization wave have seen them increasingly involved in the exchange of goods.

Already aggregated data show that the BRICs and other competitors are gaining strength over Europe and are expanding into those regions where EU27 had the primacy. This is not reassuring news for the political agenda of a Union which aims to create an environment of security, stability and prosperity with its immediate neighbours by land or sea.

Our findings are policy relevant (in terms of trade policy) when we look at the results distinguishing among types of goods traded. The EU continues to be the main destination largely for primary commodities and this is particularly true when looking at its eastern borders. Capital goods, i.e. products which are more likely to embody knowledge, are still imported primarily from the “old” member states but ENCs export them mainly to the emerging economies. When looking at semi-finished products, the geographical map for understanding the creation of value, for products which need further processing or assembly, include Europe, which in any case plays a more important role in selling rather than purchasing.

If these results can be attributed to different regulations for the free transnational movement of goods and therefore ENC goods, more than primary ones, find easier access to markets in non EU countries then the urgency of Deep and Comprehensive Free Trade Agreements that the EU is currently engaged in, or proposing to Ukraine, Moldova, Georgia, Armenia, Jordan, Egypt, Tunisia and Morocco, as part of the European Neighbourhood Policy, is clear.

Also from the point of view of single neighbouring countries the policy implications of the results here discussed clearly emerge. There are well known risks (political and economic, Collier, 2002) in concentrating exports on a few primary commodities; it exposes a country to the negative effects of the unfavourable characteristics of world demand and negative supply side features of these primary products. Also concentrating the entire export activity to a few destinations imposes risks for its continuity. We have analyzed both geographical and sectorial diversification separately and also combining the two pieces of information. We know which are the best EU27 and world partners for all the 15 countries bordering the European Union. Little has changed over time and most of countries continue to trade chiefly with an EU member state. But the degree of trade concentration where energy or other primary goods are the main export product, is very high. This is the case of Algeria, Armenia, Azerbaijan, Belarus, Libya, Syria and Ukraine. What is more, EU neighbours show better export differentiation in markets other than the EU.