

# Towards greater economic integration

The European Union's financial  
assistance, trade policy  
and investments for  
the New Independent States





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# Introduction

The New Independent States (NIS) are undergoing an unprecedented transition process, orientating their economies away from planned towards markets economies.

The European Union is supporting the multifaceted transition through a wide variety of measures, aiming at, above all, a sounder integration of the NIS into the international economic system.

Figures and facts help the understanding of the role of the EU in the NIS. The European Commission has therefore decided to update its previous publication on the European Union's commercial policy and assistance towards the NIS, including a new chapter on foreign direct investment in the region.

In order to show the importance attached to these issues, the EU's policy is presented in comparison with those practised by our main western partners, the United States and Japan.

As the data in this brochure show, the European Union has become a major trading partner of the NIS in a short period of time. The European Union is, by far, their main provider of bilateral assistance. Foreign direct investment has started to pour into the region, with strategic investors originating in the European Union playing an important role in upgrading the economies.

It is the aim of the European Commission to carry these policies even further, with a particular emphasis on opening markets, promoting trade and investment and enhancing assistance.

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## Executive summary

Bilateral economic relations between the European Union and the New Independent States (NIS) are based on three main pillars: trade policy, assistance and foreign direct investment. On all three counts the European Union and its Member States are the most important partner of the NIS. The European Union is the main customer and main supplier of the NIS. Together with its Member States the European Union provides by far the largest share of assistance to the countries of central and eastern Europe. Foreign direct investment originating in the Member States of the European Union takes an important stake in the overall inflows into the region.

For reasons of statistical consistency, all figures in this document concerning the European Union refer to the European Union of the fifteen, including Austria, Sweden and Finland even before 1995.

### European Union trade with the New Independent States

The European Union is the NIS' most important Western trading partner, having taken more than ECU 25 billion worth of imports from the NIS in 1995. This accounts for more than 33 per cent of the NIS' total exports, ranking the EU second to intra-NIS trade.

Trade between the European Union and the NIS has been growing since 1989. EU imports from the NIS have grown by more than 33 per cent since the 1989 level and EU exports to the NIS reached a growth rate of over 25 per cent over the same period. The NIS as a group are running a big trade surplus with the European Union.

By the end of 1996, the European Union had signed bilateral Partnership and Cooperation Agreements with ten NIS. As soon as they enter into force, they will boost existing links and grant NIS products even better access to the European market.

While Russia is trying to push ahead with regional integration, visible results are so far rare. Russia's share of exports to non-NIS countries has been almost 60 per cent in 1995. Ukrainian trade flows are shifting from the NIS to the non-NIS zone, and in particular to the EU. Growth in exports to non-NIS countries increased by almost 24 per cent from 1994 to 1995, whereas exports to other NIS have not been progressing.

The outlook for trade development is not very promising for 1997. While Russia has reached a front rank in the list of main trading partners of the EU (Russia ranks sixth as regards EU imports and fifth as regards EU exports), high rates of growth in NIS exports will probably not persist. Exports to the European Union, the NIS' major trading partner, are predicted to increase in 1997, however the NIS seem unable to profit from this. Growth rates in NIS exports are likely to be much lower in 1997 than they were in 1995.

### Assistance to the New Independent States

The benefits that the NIS derive from European Union assistance are similar. Between 1990 and 1995 the European Union and its Member States provided ECU 72.7 billion in aid out of a total of ECU 123.2 billion, or 59 per cent. If the aid is broken down by category it becomes clear that the European Union and its Member States are generally the principal providers of aid to the NIS: 49 per cent of food aid; ECU 32.7 billion in export credits out of a bilateral total of ECU 45.4 billion; 89.2 per cent of the strategic aid and 58.6 per cent of the technical assistance given, mainly via the Tacis Programme.

### Foreign investment in the New Independent States

Foreign direct investment (FDI) is a major vehicle for developing a strong, dynamic private sector. It is essential to ensure successful transition to a market-based economic system and integration into the world market. In 1995, FDI inflows into the region continued to increase. However, the cumulative amount of FDI in the region remains small. Strategic investors originating in the Member States of the European Union play a major role, accounting for up to 50 per cent of total FDI inflows in individual NIS countries.



# European Union trade with the New Independent States

## The NIS' largest Western trading partner

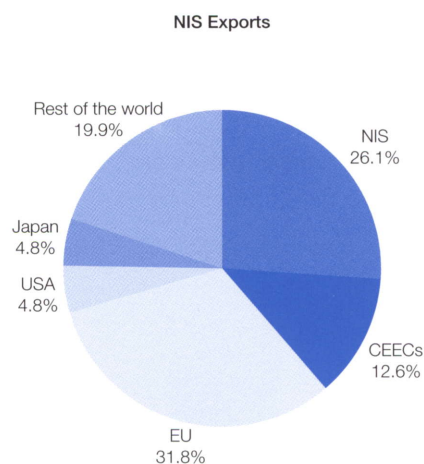
The European Union is the New Independent States' (NIS) largest trading partner outside the former Soviet Union.

In 1989, the Soviet Union had its major trade links within the Council for Mutual Economic Assistance (CMEA). All Soviet republics were closely integrated in the economic planning system of the Soviet Union, and none traded extensively with the rest of the world.

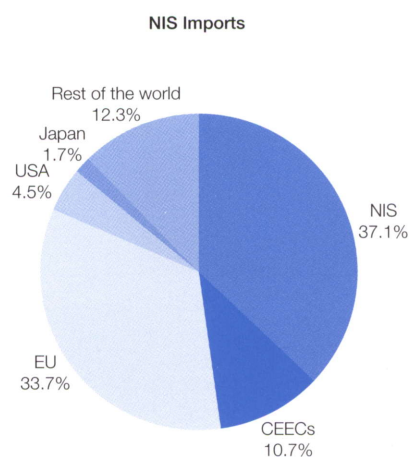
After the break-up of the Soviet Union, 15 states emerged and gained independence. The three Baltic states swiftly redirected their foreign trade towards the European Union. Most of the twelve New Independent States - Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan - tried to open their economies and reorient their exports towards world markets, mainly towards the EU.

Today, the European Union accounts for more than 32 per cent of total NIS exports and 34 per cent of total NIS imports. Following intra-NIS trade, the EU ranks first as regards NIS imports and exports.

## Structure of the NIS' external trade in 1995 (%)



Source: IMF



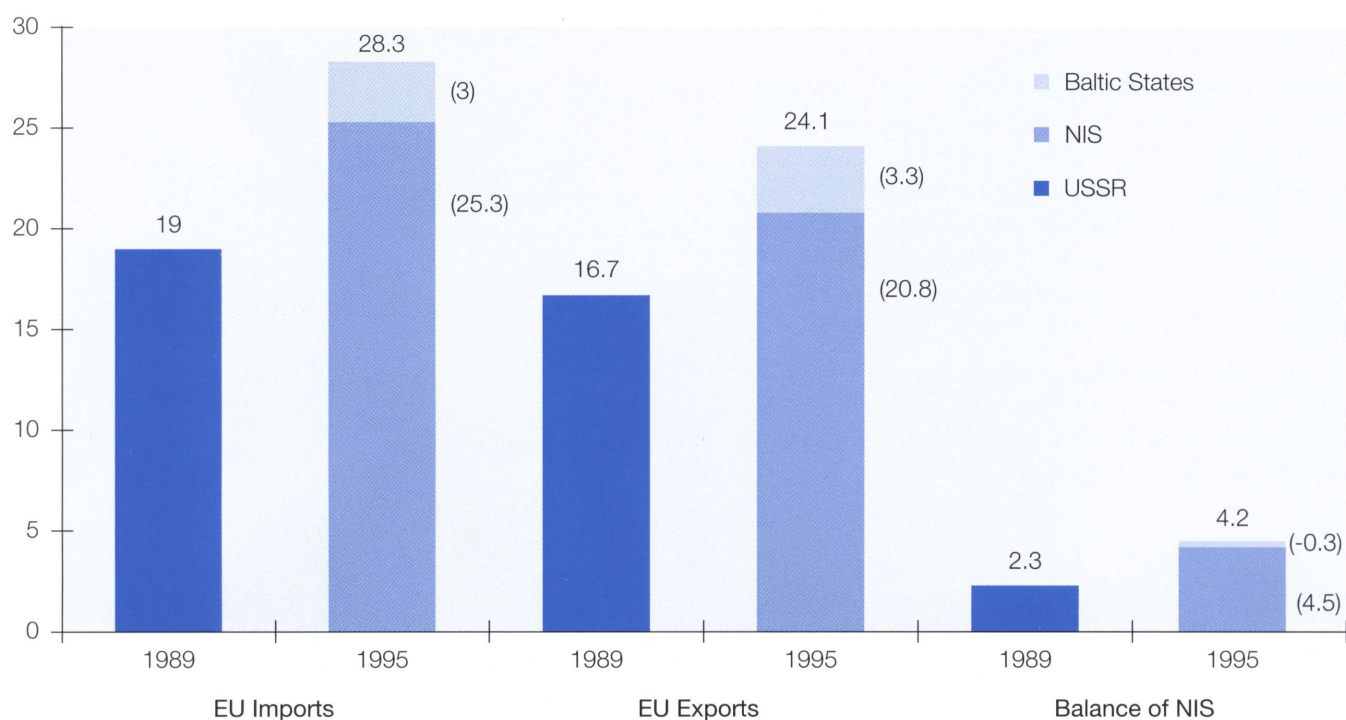
Source: IMF

Trade between the EU and the NIS has been accelerating. Between 1989 and 1995, exports of the NIS to the EU grew by 33.1 per cent, reaching a value of ECU 25.3 billion in 1995<sup>1</sup>. This produced a surplus of ECU 4.5 billion in favour of the NIS, which is an increase of nearly 100 per cent over the 1989 level. However, the trade surplus

peaked in 1994, where it stood at ECU 6.0 billion - having increased 164% over 1989.

The main reason for the trade imbalance between the European Union and the NIS is the European Union's purchases of energy and minerals, mainly from Russia.

### The pattern of trade between the former Soviet Union and the European Union between 1989 and 1995 (ECU billion)



### The pattern of trade between the former Soviet Union and the European Union between 1989 and 1995 (ECU billion)

	EU(15) Imports from			EU(15) Exports to			Balance of NIS	
	1989	1995	% increase 1989-1995	1989	1995	% increase 1989-1995	EU imports	EU exports
<b>USSR</b>	19			16.7			2.3	
<b>NIS</b>		25.3	33.1		20.8	24.5		4.5
<b>NIS + Baltic States</b>		28.3	48.9		24.1	44.3		4.2

Source : Eurostat-Comext

<sup>1</sup> Statistical data for the former Soviet Union always include the NIS plus Baltic States. Unfortunately, it is impossible to obtain data for the twelve NIS as such before 1992.



The individual NIS have reported widely varied experiences in their foreign trade. While few faced sharp declines, most NIS saw rapid growth rates in foreign trade in 1995, especially Kyrgyzstan, Armenia and Georgia<sup>1</sup>. Trade with the EU is developing dynamically, especially for Moldova, Armenia, Azerbaijan, albeit from a very low base.

Of the NIS, Russia is by far the EU's main trading partner. It accounts for 87 per cent of total EU imports and 77 per cent of total EU exports to the NIS in 1995. Ukraine followed with a share of 6 per cent of EU imports from the NIS accounting for ECU 1.48 billion. Belarus, Uzbekistan and Kazakhstan took 2.2 per cent, 2.0 per cent and 1.4 per cent of EU imports from the NIS in 1995. On the other hand, Germany was the main importer from the NIS, accounting for 31.5 per cent. Italy followed with a share of 20.3 per cent and France with 12.1 per cent.

While energy-rich Russia is running a big surplus with the EU, most other NIS face deficits in their trade balance with the EU.

NIS exports to the EU were evenly divided between primary and manufactured goods (40 per cent each), while the remaining 20 per cent was covered by other non-classified goods in 1995. In 1991, NIS exports of primary goods to the EU, in particular mineral fuels, still accounted for 56 per cent whereas those of manufactured products (especially non-ferrous metals and iron and steel products) for only 21 per cent.

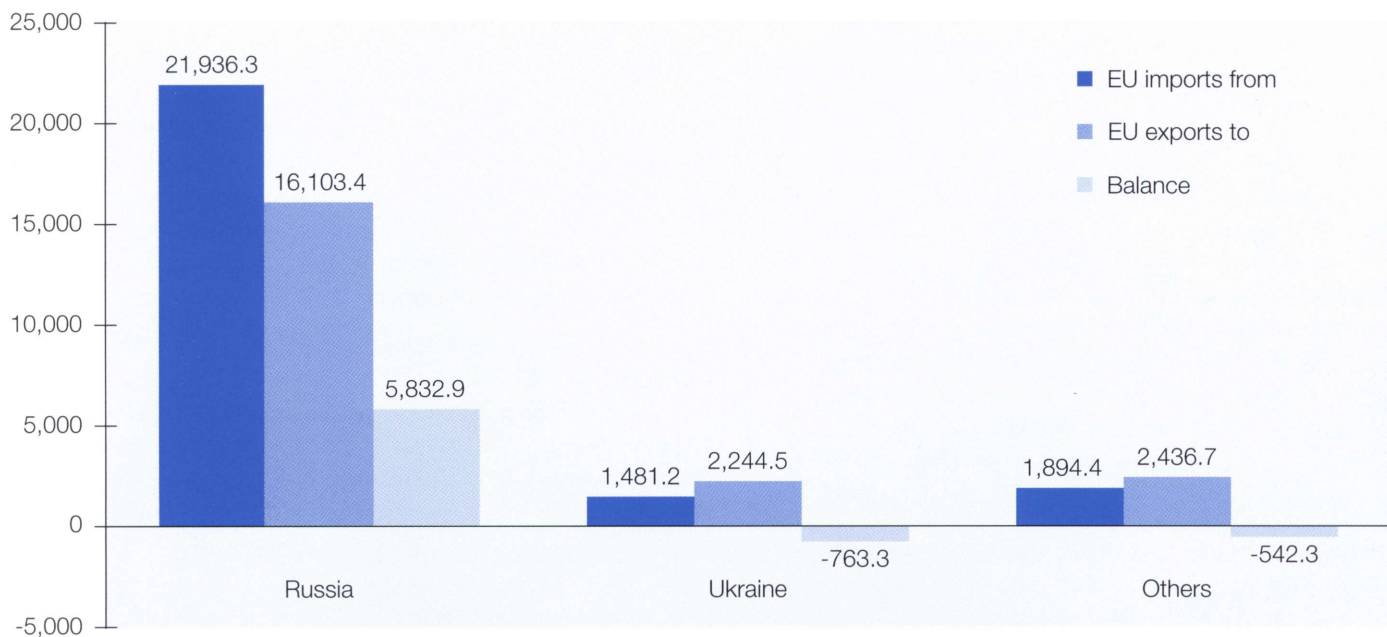
In contrast, the share of manufactured products in NIS imports from the EU fell from 80 per cent in 1991 to 73 per cent in 1995. Primary products increased from a share of 15 per cent in 1991 to 24 per cent in 1995, mainly due to sharp increases in food and beverages.

### Trends in trade between the European Union and the New Independent States 1993-1995 (ECU million)

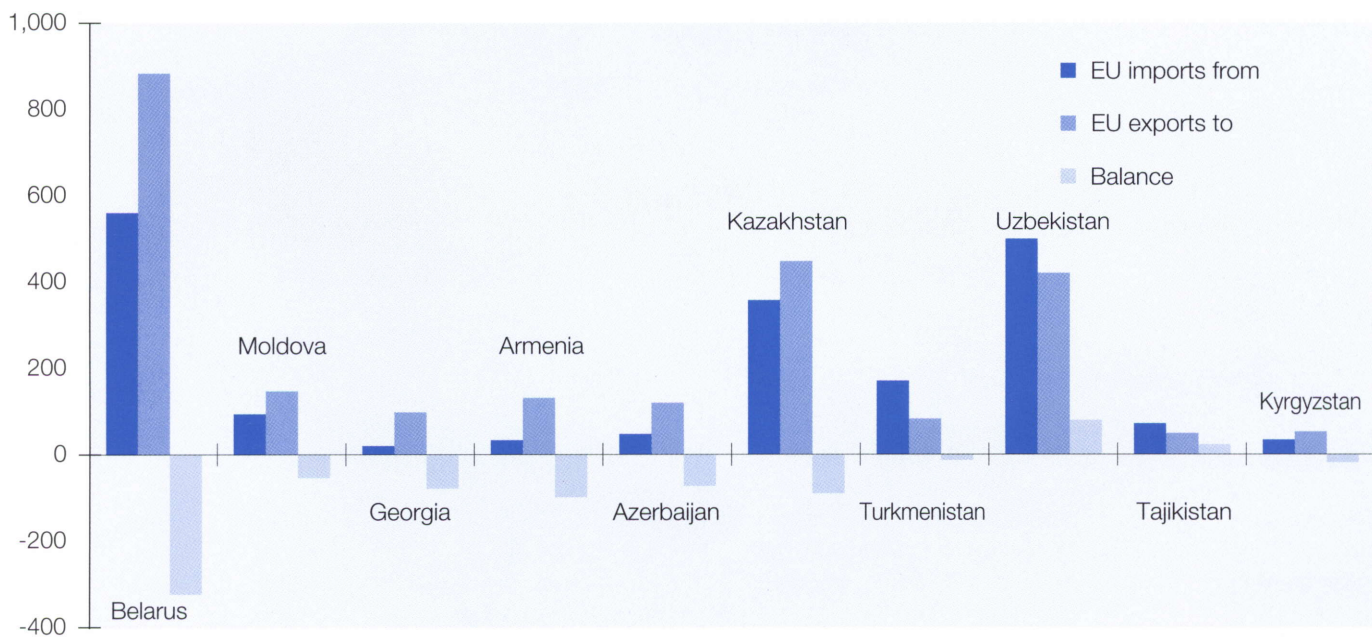
	EU imports from			EU exports to			Balance EU imports EU exports	
	1993	1995	% increase 1993-1995	1993	1995	% increase 1993-1995	1993	1995
Russia	17,615.4	21,936.3	24.5	13,149.6	16,103.4	22.5	4,465.8	5,832.9
Ukraine	1,011.7	1,481.2	46.4	1,570.4	2,244.5	42.9	-558.7	-763.3
Belarus	275	561.6	104.2	583	884.5	51.7	-308	-322.9
Moldova	27.2	95	249.3	67.2	148	120.9	-40	-53
Georgia	38.8	20.9	-46.1	89.5	98.8	10.4	-50.7	-77.9
Armenia	14.8	34	129.7	55	132.1	140.2	-40.2	-98.1
Azerbaijan	39.2	48.1	22.7	61.3	120.4	96.7	-22	-72.4
Kazakhstan	317	358.3	13	678.8	448.1	-34	-361.8	-89.9
Turkmenistan	159.2	171.2	7.5	120.3	83	-31	38.9	88.2
Uzbekistan	428.6	499.6	16.6	211.1	420.2	99.1	217.5	79.4
Tajikistan	62.4	72	15.4	58.3	49	-15.9	4.21	23
Kyrgyzstan	8	33.9	323.8	26.6	52.6	97.7	-18.6	-18.7
<b>NIS Total</b>	<b>19,997.3</b>	<b>25,312.1</b>	<b>26.6</b>	<b>16,671.1</b>	<b>20,784.6</b>	<b>24.7</b>	<b>3,326.4</b>	<b>4,527.3</b>

<sup>1</sup> UN/ECE

**Balance of trade of the NIS with the EU in 1995 (ECU million)**



**Balance of trade of the NIS except Russia and Ukraine in 1995 (ECU million)**



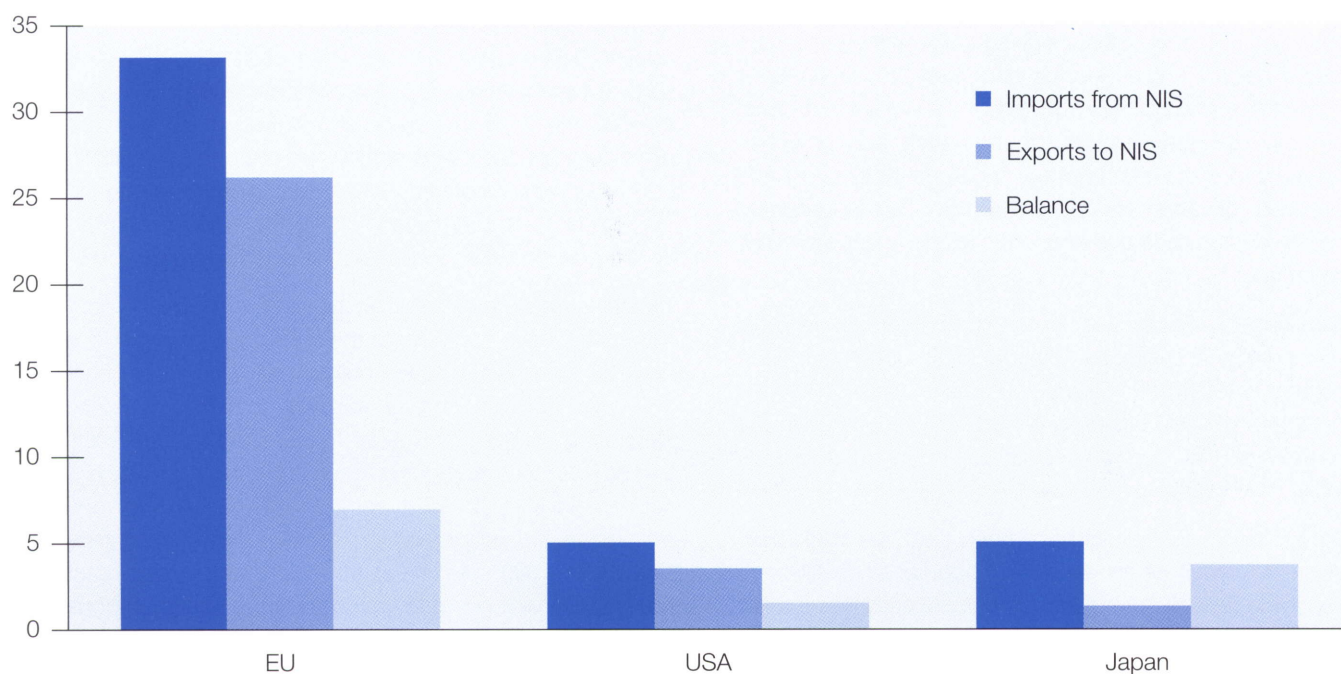
Source: Eurostat-Comext

### Comparison with other western nations

The European Union does more trade with the NIS than all other western partners put together.

Its imports from the NIS were worth US\$ 33 billion in 1995, compared to US\$ 5 billion each for the USA and Japan.

Moreover, the NIS' trade surplus with the European Union was a significant US\$ 6.95 billion in 1995. Its surplus with the USA was only US\$ 1.51 billion. The surplus with Japan amounted to US\$ 3.73 billion.

**NIS trade with the EU, the USA and Japan in 1995 (US\$ billion)****NIS trade with the EU, the USA and Japan in 1993-1995 (US\$ billion)**

	Imports from NIS		Exports to NIS		Balance of NIS (imports - exports)	
	1993	1995	1993	1995	1993	1995
<b>EU (15)</b>	23.55	33.15	19.38	26.2	4.17	6.95
<b>USA</b>	2.22	5.03	3.84	3.52	-1.62	1.51
<b>Japan</b>	2.99	5.06	1.67	1.33	1.32	3.73

Source: Eurostat, based on IMF DOTS

## Economic cooperation and integration among the NIS

Following the break-up of the Soviet Union, the successor states gained independence and tried to unravel their intertwined economies. Yet, the transformation from a centrally planned economy to a market economy has proved very difficult and painful, and some NIS have made a series of attempts to provide for an appropriate framework for trade and economic relations between their countries.

The Russian Federation is trying to reinforce regional cooperation and greater integration among the NIS. A number of bilateral free trade agreements were concluded in 1993 and 1994. To push ahead with integration in the context of the Commonwealth of Independent States (CIS), new treaties were signed.

So far, the visible results have been few. The implementation record of all agreements - bilateral or multilateral, free trade agreements, customs unions, common market agreements and economic unions - has not been very encouraging. Intra-NIS trade seems to have grown little in value and has probably contracted further in volume <sup>1</sup>.

Russia's exports have expanded steadily in the last three years with trade flows orientating increasingly to non-NIS

partners. Russian trade with NIS partners decreased from 25.9 per cent of total trade in 1993 to 22.7 per cent in 1995. While exports to the NIS have only recently begun to grow again following stagnation in 1994, NIS imports advance more rapidly. Though Russia is running an overall surplus (also with the EU), it recorded a trade deficit with the NIS in 1995. The trend in redirection of crude oil, petroleum products and natural gas exports from NIS to non-NIS countries continued in 1995. While oil exports to the non-NIS zone remained virtually the same in 1995 as in 1994, oil deliveries to the NIS dropped by 22 per cent.

Ukrainian trade flows are shifting from the NIS to the non-NIS zone, and in particular to the EU. Growth in exports to non-NIS countries increased by almost 24 per cent from 1994 to 1995, whereas exports to other NIS are stagnating. However, Russia remains by far the main trading partner. As regards trade links as a whole, NIS imports were up to 67.4 per cent of total imports and exports to the NIS made up to 58.1 per cent of total exports in 1995. Ukraine is struggling with a significant trade deficit which is due mainly to heavy energy imports from Russia and Turkmenistan.

Trade data should however be viewed with caution as they often reflect only part of the real situation. There is a substantial amount of unregistered and barter trade, which experts estimate at about 30 per cent.

<sup>1</sup> Economic Survey for Europe 1995-1996

## External trade of Russia and Ukraine (US\$ billion)

	Exports to				Imports from				Balance				
	1993	1994	1995	% increase 1993-1994 1994-1995	1993	1994	1995	% increase 1993-1994 1994-1995	1993	1994	1995		
<b>Russia</b>													
NIS	15.4	14.9	15.6	-3.2	4.7	11.5	13.5	16.7	17.4	23.7	3.9	1.4	-1.1
non-NIS	44.3	53.2	66.0	20.1	24.1	32.8*	36.9*	44.1*	12.5	19.5	11.5	16.3	21.9
<b>Total</b>	<b>59.7</b>	<b>68.1</b>	<b>81.6</b>	<b>14.1</b>	<b>19.8</b>	<b>44.3</b>	<b>50.4</b>	<b>60.8</b>	<b>13.8</b>	<b>20.6</b>	<b>15.4</b>	<b>17.7</b>	<b>20.8</b>
<b>Ukraine</b>													
NIS	7.6	7.5	7.9	-1.3	5.3	10.6	10.1	10.8	-4.7	6.9	-3.0	-2.6	-2.9
non-NIS	5.2	4.6	5.7	-11.5	23.9	4.7	4.3	5.2	-8.5	20.9	0.5	0.3	0.5
<b>Total</b>	<b>12.8</b>	<b>12.1</b>	<b>13.6</b>	<b>-5.5</b>	<b>12.4</b>	<b>15.3</b>	<b>14.4</b>	<b>16.0</b>	<b>-5.9</b>	<b>11.1</b>	<b>-2.5</b>	<b>-2.3</b>	<b>-2.4</b>

Sources: for Russia, Russian Economic Trends 1996, Vol. 5, No. 1; for Ukraine, IMF

\* Figures include estimates of non-registered shuttle-trade and humanitarian aid

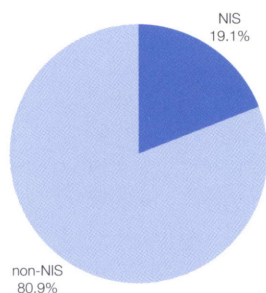
## Trade with NIS as % of total trade\*

	1993		1994		1995	
	Exports	Imports	Exports	Imports	Exports	Imports
<b>Ukraine</b>	59.4	69.3	62.0	70.1	58.1	67.5
<b>Russia</b>	25.8	26.0	21.9	26.8	19.1	27.5

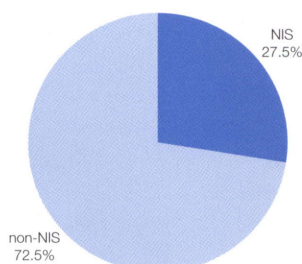
\* officially registered trade

Source: Russian Economic Trends 1996, Vol. 5, No. 1

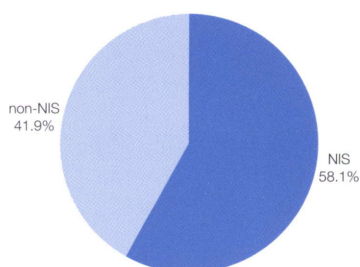
Russian exports 1995



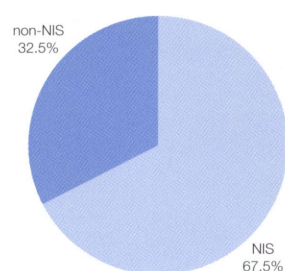
Russian imports 1995



Ukrainian exports 1995



Ukrainian imports 1995



Russia is taking the greater part in almost all the NIS' external trade statistics rubrique "trade with transition countries". 77.5 per cent of Belarussian and 94.4 per cent of Kazakhstan's imports from transition countries is accounted for by Russia in 1995. 93.7 per cent of Kyrgyz and 82.2 per cent of Uzbek exports to transition countries went to Russia in 1995. Yet, one should not ignore the fact that trade among the NIS mostly takes the form of shuttle and other non-registered trade, which does not enter the statistics. But even taking into account that the statistics do not wholly reflect real trade flows, the general trade pattern of intra-NIS trade is clearly visible: all other NIS depend heavily on Russia. The few exceptions confirm this rule, though they hint at new regional orientations: Azerbaijan's biggest export customer is neighbouring Iran, Kyrgyzstan's biggest export client is neighbouring China.

Trade with central and eastern European transition countries is growing again.

The share of Russia's trade with non-NIS taken by the central and eastern European transition countries (Hungary, Poland, the Czech Republic, Slovakia, Bulgaria, Romania) has begun to grow again after a long decline. It rose at 11.6 per cent in 1994 and 12.7 per cent in 1995. Russia's exports to the CEECs rose by more than 38 per cent in 1995.

Russia faces a significant trade surplus with all CEECs. Yet, this surplus is shrinking due to the fact that imports from CEECs are growing faster than the Russian exports to the region. Over 70 per cent of Russian exports are fuels. Over one third of imports from CEEC are foodstuffs, beverages and tobacco. Major CEEC trading partners are Poland (26 per cent), Hungary (21 per cent) and Slovakia (Czech Republic and Slovakia together 35 per cent).

## Agreements

The new bilateral Partnership and Cooperation Agreements will strengthen economic and political cooperation between the European Union and the individual partner countries. They will sustain the development of trade and investment and harmonious relations between the EU and the NIS.

Although these Agreements are diverse, reflecting the differences between the partner countries themselves, each establishes a strong and comprehensive political and economic partnership between the EU and the NIS covering in particular trade in goods, a political dialogue as well as a variety of trade-related matters.

The PCAs are based on shared principles and objectives: respect for the rule of law and human rights, the development of political freedoms and the establishment of a functioning market economy. Furthermore, they aim at supporting the integration of the NIS into the world economy.

The European Union's Tacis Programme is the major tool to facilitate cooperation under each Agreement. It provides grant finance to support the partner countries' efforts to consolidate democracy and to complete the transition to the market economy.

So far, ten NIS have already signed the PCAs and await ratifications. They will replace the 1989 Agreement on Trade and Commercial Economic Cooperation, which was drawn up between the European Communities and the entire Soviet Union.

Because of the need to promote rapidly the development of trade relations between the EU and the NIS, it has been decided to implement the trade and trade-related provisions of the PCA by means of Interim Agreements. This will allow the parties to benefit from the trade and commercial provisions of the PCAs at the earliest possible juncture.

So far, the Interim Agreements with Russia, Ukraine and Moldova have already entered into force. The Interim Agreements with Belarus, Kazakhstan, Kyrgyzstan, Armenia, Uzbekistan and Georgia are signed and await conclusion. The Interim Agreement with Azerbaijan has been initialled.

## Trade policy

The European Union market is already extremely open to imports from the NIS. Many of the products which the NIS export to the EU are subject to low or zero-rated customs duties, thus much of their merchandise trade is already virtually free of restrictions. Indeed, even though the PCA do not offer preferential treatment, this did not prevent the EU's trade with the NIS from rising more than 26% between 1993 and 1995, the first year in which trade with the NIS was registered individually. In the case of Armenia, for example, the growth in exports rocketed by more than 140 per cent.

The European Union already granted the former Soviet Union MFN (Most Favoured Nation) status in the 1989 Agreement on Trade and Commercial Economic Cooperation. The new generation of bilateral Partnership and Cooperation Agreements will confirm this.

Furthermore, the European Union has given all NIS access to the Generalised System of Preferences (GSP). The GSP offers tariff reductions, or in some cases duty-free access, for manufactured goods and certain agricultural exports as well. Approximately 10 per cent of imports from the NIS are eligible for GSP treatment. However if optimum use is made of the GSP by the NIS, this may result in an even lower average tariff rate on industrial products as a whole.

Even disregarding the GSP, 83 per cent of imports from Russia, for example, are free of duty. The weighted average tariff on imports from Russia is under 1 per cent.

Specific quantitative restrictions which apply only to state-trading countries were lifted on 1 August 1991.

ECCS products have been liberalised after December 1995. Therefore there are voluntary restriction agreements with Russia and Kazakhstan, but only on some products. Voluntary restriction agreements also exist with all NIS on textile and clothing products.

Non-specific quantitative restrictions applying to the NIS were lifted on 15 March 1994.

The safeguard clause has so far only been used once with Russia, in an aluminium case.

Anti-dumping measures are in force for eleven varieties of Russian goods as of 1 September 1996. Four investigations are under way. If the investigations culminate in anti-dumping measures, the volume affected would represent less than 1 per cent of total trade. In the case of Ukraine, seven anti-dumping measures are in force and three investigations are under way. They too affect less than 1 per cent of total bilateral trade.

Antidumping measures are an integral part of the rules of multilateral trade. As long as the NIS are not recognised as market economies the rules applicable refer to those for state trading countries (reconstitution of real value). However, the European Commission has indicated to the Ukrainian government that there is a possibility of

individual treatment for producers who are able to prove that they function without state intervention.

Bilateral European Union, US and Japanese trade policy with the NIS stood as follows at the beginning of 1996.

### European Union, United States and Japan - trading preferences to the New Independent States

	Partnership and Cooperation Agreement	European Union Bilateral agreement in force	United States			Japan	
			MFN/GSP	MFN	GSP	MFN	GSP
Russian Federation	signed	Interim Agreement 1.2.1996	Yes	Yes	Yes	Yes	to be offered
Ukraine	signed	Interim Agreement 1.2.1996	Yes	Yes	Yes	Yes	Yes
Belarus	signed	Covered by TCA with ex-USSR Interim Agreement signed	Yes	Yes	Yes	Yes	Yes
Moldova	signed	Interim Agreement 1.5.1996	Yes	Yes	Yes	Yes	Yes
Kazakhstan	signed	Covered by TCA with ex-USSR Interim Agreement signed	Yes	Yes	Yes	Yes	Yes
Kyrgyzstan	signed	Covered by TCA with ex-USSR Interim Agreement signed	Yes	Yes	Yes	Yes	to be offered
Turkmenistan	initialled	Covered by TCA with ex-USSR	Yes	Yes	–	Yes	to be offered
Uzbekistan	signed	Covered by TCA with ex-USSR Interim Agreement signed	Yes	Yes	Yes	Yes	to be offered
Tajikistan	–	Covered by TCA with ex-USSR	Yes	Yes	–	Yes	to be offered
Armenia	signed	Covered by TCA with ex-USSR Interim Agreement signed	Yes	Yes	Yes	Yes	Yes
Azerbaijan	signed	Covered by TCA with ex-USSR Interim Agreement initialled	Yes	Yes	–	Yes	No
Georgia	signed	Covered by TCA with ex-USSR Interim Agreement signed	Yes	Yes	–	Yes	Yes

Source: Services of the Commission



## The future outlook

The NIS have significantly increased their share of imports into the European Union since 1992. The NIS as a group now account for more than 4 per cent of imports into the EU from third countries. Of particular prominence is Russia which ranks sixth among the list of the EU's main trading partners in 1995, ahead of Poland (7), Taiwan (8), Canada (9) and South Korea (10).

Ukraine also ranks amongst the major EU trading partners. Belarus, Uzbekistan, Kazakhstan, Turkmenistan, Moldova, Tajikistan, Azerbaijan, Kyrgyzstan and Armenia follow in this order of listing.

### Main trading partners of the EU (volume in %)

Rank 1995	Imports in origin from	1992	1993	1994	1995
1	USA	20.1	19.3	19.3	19.0
2	Japan	12.2	11.1	10.4	10.0
6	Russia	2.3	3.7	4.1	4.0
49	Ukraine	0.1	0.2	0.3	0.3

Rank 1995	Exports to	1992	1993	1994	1995
1	USA	16.5	17.0	17.2	15.7
3	Japan	4.6	4.6	4.8	4.9
6	Russia	2.7	2.5	2.4	2.4
46	Ukraine	0.2	0.3	0.3	0.3

Source : Comtrade Comext

The outlook for growth in NIS trade is not very promising in the short term.

Current economic predictions on the external trade of the European Union for 1997 hint at a difficult period to come.

In 1995, NIS exports grew by an impressive 21.8 per cent. This was due mainly to accelerated growth in exports to developing countries, mainly Asian ones. The NIS' growth in market share in EU imports seems now to be consolidating. The imports from the NIS to the European Union experienced a slight increase in volume in 1995. Although the NIS did not feel the effects of the marginal decline in their external trade with the European Union in 1993, they were unable to increase their share of EU imports in 1995 any further.

Growth of NIS exports has probably decelerated

significantly in 1996. Yet, the NIS' growth rate was well above the growth rate of EU exports. The disappointing economic situation which prevailed in the European Union, the NIS' major non-NIS trading partner, has probably affected declining growth rates in NIS imports, too.

For 1997, the predictions indicate an improvement of the economic situation in the EU, with an increase in European Union imports of 5.3 per cent. If the predictions reflected real developments, which is never completely the case, the NIS would seem to be unable to profit from it, since a further slowdown in their export growth in 1997 is expected. Pushing ahead with economic reforms and restructuring the economies are crucial to enhance competitiveness and increase the NIS' share in world markets.

### Growth in international trade (volume in %)

		1995	1996 (estimates)	1997 (forecast)
<b>Imports</b>	of the EU	6.2	3	5.3
	of the rest of the world (-EU)	11	8.1	8.1
	of the NIS	-3.3	6.8	10.9
<b>Exports</b>	of the EU	7.3	3.8	6
	of the rest of the world (-EU)	10.9	6.9	8
	of the NIS	21.8	4.3	3.3

Source: Services of the Commission

## Assistance to the New Independent States

Since the collapse of the Soviet Union, the European Union and its Member States have been by far the greatest source of aid to the NIS.

In the period from September 1990 to January 1996, the international community and its major donors provided the NIS countries with at least ECU 123 billion in assistance.

The European Union provided some 59 per cent of this bilateral aid in the period 1990-1995. In comparison, the United States provided a little less than 14 per cent of the total and Japan provided just over 5 per cent of the total.

Germany is the largest individual contributor in the European Union, notably because of the export credits and the strategic assistance it accorded the former Soviet Union following the German unification.

### Assistance to the New Independent States by major donors in the period 30 September 1990 to 1 January 1996 (ECU billion)

	ECU billion	%
European Union	5.1	4.1
Member States	67.6	54.9
United States	17.1	13.9
Japan	6.3	5.1
Total (without IFI)	96.1	78
IFI	27.1	22
<b>Total</b>	<b>123.2</b>	<b>100</b>

Source : Services of the Commission

### Breakdown of assistance by sector

The European Union and its Member States have given the NIS more than ECU 2.66 billion in humanitarian and food aid (48.8 per cent of the bilateral total). The United States has provided ECU 2.57 billion (47.1 per cent) and Japan ECU 224 million (4.1 per cent).

The European Union and its Member States have also been at the forefront of technical assistance, contributing over ECU 3.4 billion (59 per cent of the total). The European Union alone has provided ECU 2.3 billion, (almost 40 per cent) of the bilateral total, primarily through its Tacis Programme. The United States has provided ECU 2.2 billion (38.7 per cent) and Japan 2.7 per cent.

Concerning credits and credit guarantees, the European Union and its Member States have provided over ECU 30 billion, or 73.8 per cent of the bilateral total, with Germany alone contributing over ECU 21 billion. The United States, in comparison, has provided just over ECU 7.1 billion (17.1 per cent, excluding IFIs) and Japan a little more than ECU 4.5 billion (11 per cent).

In the area of strategic assistance (that is, financial help for the withdrawal of Soviet forces and the destruction of strategic missiles) the Member States (primarily Germany) have provided almost 90 per cent of a total of some ECU 10 billion and the United States, 10 per cent of this total.

**Assistance to the NIS 1990-1995 - Breakdown by sector** (ECU million)

	Food & Humanitarian aid	Technical assistance	Credits & guarantees	Strategic assistance	Debt rescheduling	Official assistance for private investment	Others	Total
European Union	735	2,268	2,135	0	0	0	0	5,138
Member States	1,926	1,098	30,625	8,782	12,326	12,744	60	67,561
United States	2,572	2,224	7,084	987	0	3,295	904	17,066
Japan	224	155	4,551	82	1,280	0	27	6,319
Total (without IFI)	5,457	5,745	44,395	9,851	13,606	16,039	991	96,084
IFI	0	460	26,660	0	0	0	0	27,120
<b>Total</b>	<b>5,457</b>	<b>6,205</b>	<b>71,055</b>	<b>9,851</b>	<b>13,606</b>	<b>16,039</b>	<b>991</b>	<b>123,204</b>

Source : Services of the Commission

## Foreign investment in the New Independent States

The NIS need significant levels of foreign investment to upgrade their economies.

Foreign direct investment (FDI) is a major vehicle for developing a strong, dynamic private sector. It is essential to ensure successful transition to a market-based economic system and integration into the world market. Strategic foreign investors not only bring debt-free capital but also know-how, technology and access to foreign markets.

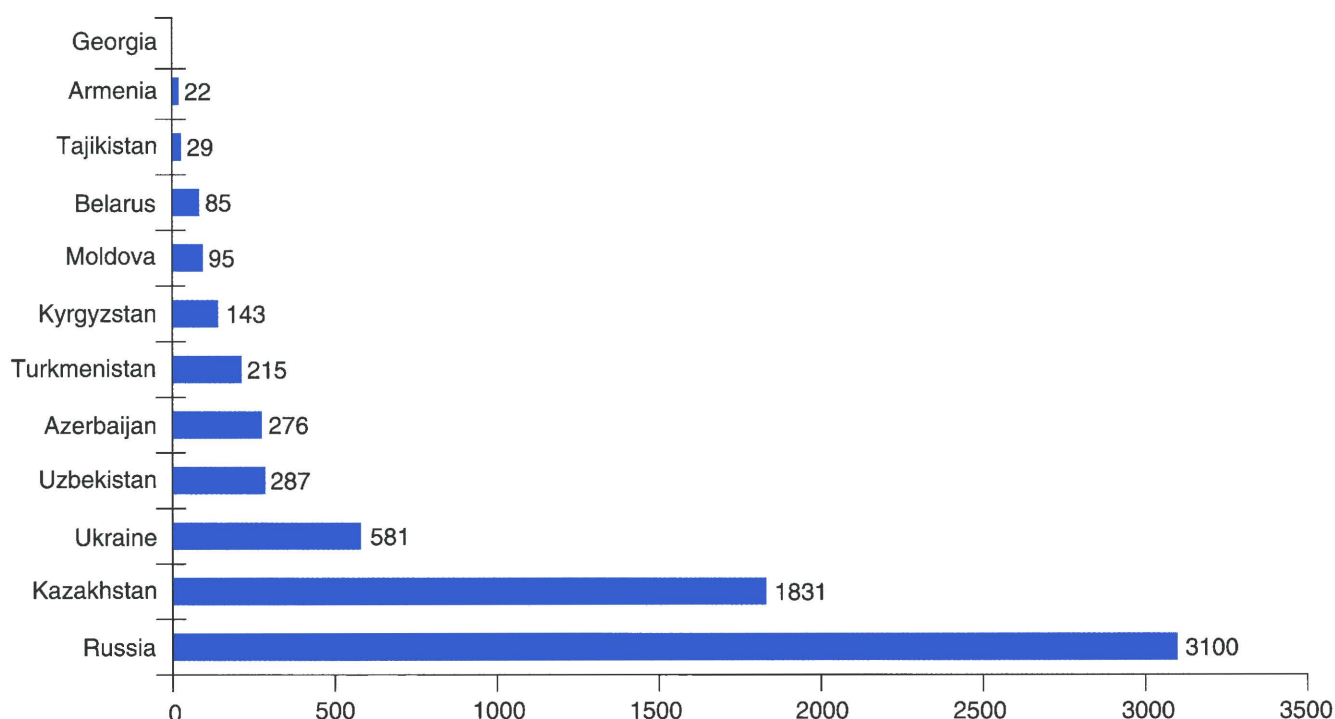
Under the socialist planned economy foreign investment was viewed with suspicion, and discouraged in the Soviet Union. Thus, only with the opening up of the NIS economies did FDI start to come into the region.

So far, FDI inflows to the NIS have been low. As a share of GDP, they can only be called marginal (0.4 per cent in the case of Russia in 1995). Although reliable FDI figures are difficult to obtain, it is nevertheless clear that investors from abroad still hesitate to enter the NIS market.

Calculating by the total amount of foreign investment to the NIS, Russia has attracted by far the largest amount of the FDI. 1995 was a successful year with foreign investment increasing by 50 per cent over the 1994 level. Total FDI stock in Russia amounted to US\$ 3.1 billion in 1995. Measured by the number of foreign investment registrations, the cumulative total soared from 1,535 at the beginning of 1991 to 21,061 in 1995. If compared to the total amount of FDI in other transition economies, Russia ranks third behind Hungary and the Czech Republic. Measured against FDI per capita, Russia lags behind Kazakhstan and Azerbaijan.

Foreign direct investment in Ukraine dropped significantly in 1994. However it began to increase again in 1995. The impact on the economy is still marginal, as FDI as a percentage of GDP accounted only for 0.4 per cent in 1995. The amount of FDI per capita stood at US\$ 2 in 1995. The central Asian republics and Azerbaijan are catching up. FDI in Kazakhstan, Uzbekistan, Azerbaijan

### Cumulative FDI in the NIS 1989-1995 (US\$ million)



Source: EBRD Transition Report 1995 and 1996

and Kyrgyzstan is comparatively small but has been growing since 1993, reaching a share of more than 10 per cent of GDP in the case of Azerbaijan. Rich natural resources make them attractive investment locations for investors who are not afraid of risk-taking.

EU enterprises are the strongest investors in Russia. EU investors account for half of all foreign investment in Russia. US companies rank second with 25 per cent,

whereas Japanese investors only took 2 per cent of total FDI stock until 1 January 1996. In Ukraine, the breakdown of total FDI by countries of origin is similar. However, Japan is hardly present, whereas the NIS, especially Russia, take an important stake of more than 5 per cent.

### Foreign direct investment in the NIS (US\$ million)

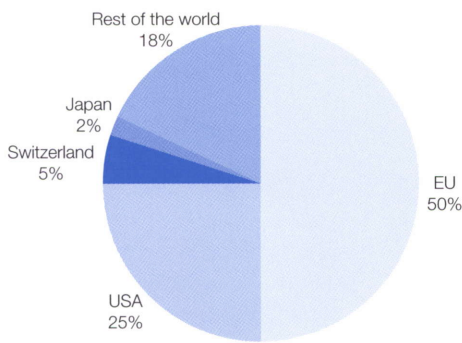
	1993	1994	1995	\$ per capita in 1995	Cumulative 1989-1995	\$ per capita cumulative	Share of GDP, 1995*
Russia	400	1000	1500	10	3100	21	0.40%
Kazakhstan	473	635	723	43	1831	110	4%
Ukraine	200	91	120	2	581	11	0.40%
Uzbekistan	48	85	120	5	287	13	1.50%
Azerbaijan	20	50	206	28	276	37	11.70%
Turkmenistan	104	100	100	na	215	54	10.6%
Kyrgyzstan	10	45	88	20	143	32	1.20%
Moldova	14	18	63	15	95	22	3.50%
Belarus		10	7	1	85	8	na
Tajikistan	9	12	13	5	29	5	na
Armenia	0	3	19	5	22	6	1.40%
Georgia		8	6	1	92	17	na
<b>Total NIS</b>	<b>1,278</b>	<b>2,057</b>	<b>2,965</b>	<b>10</b>	<b>6,756</b>	<b>24</b>	<b>0.60%</b>

\* GDP at PPP exchange rates

In Kazakhstan, which attracted US\$ 1.8 billion of total foreign investment and ranks second to Russia, US companies are taking the leading role (65 per cent). With about 75 per cent of all foreign direct investment going to the gas and petroleum industry, US companies clearly dominate among foreign investors. European Union investors account for only 12 per cent, NIS enterprises for 4 per cent and Japanese companies for 2 per cent of total FDI as of 1 January 1996.

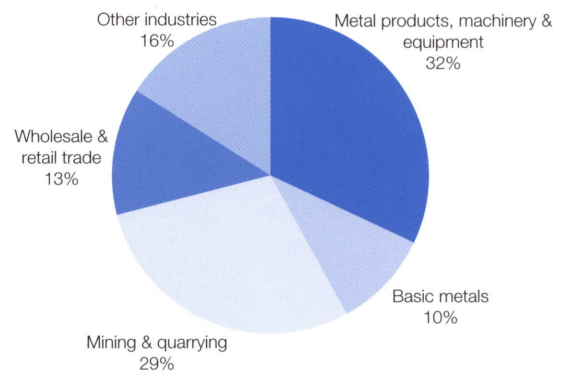
FDI is still concentrated on a few sectors. Metals, engineering and mining attract more than two thirds of all FDI in Russia. Chemicals and petrochemicals, fuels and engineering account for almost two thirds of total FDI in Ukraine. FDI inflows into Kazakhstan and central Asia have focussed on the gas and petroleum sector.

**FDI in Russia**  
(breakdown of stock as of 1 Jan. 1996)



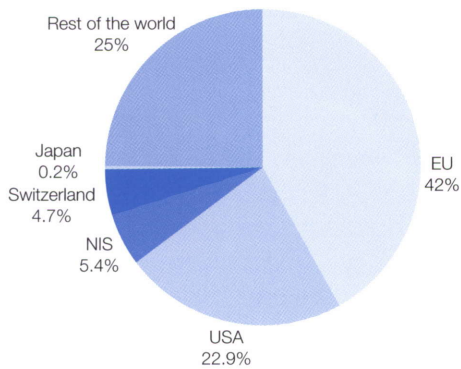
Source: UN/ECOSOC

**FDI in Russia (breakdown by industry as of 1 Jan. 1996)**



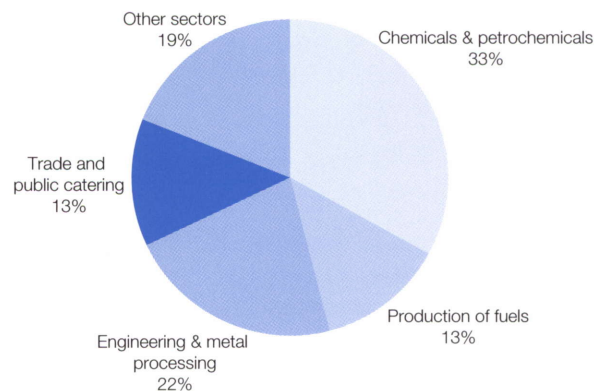
Source: UN/ECOSOC

**FDI in Ukraine (breakdown of stock as of 1 Jan. 1996)**



Source: UN/ECOSOC

**FDI in Ukraine (breakdown by industry as of 1 Jan. 1996)**



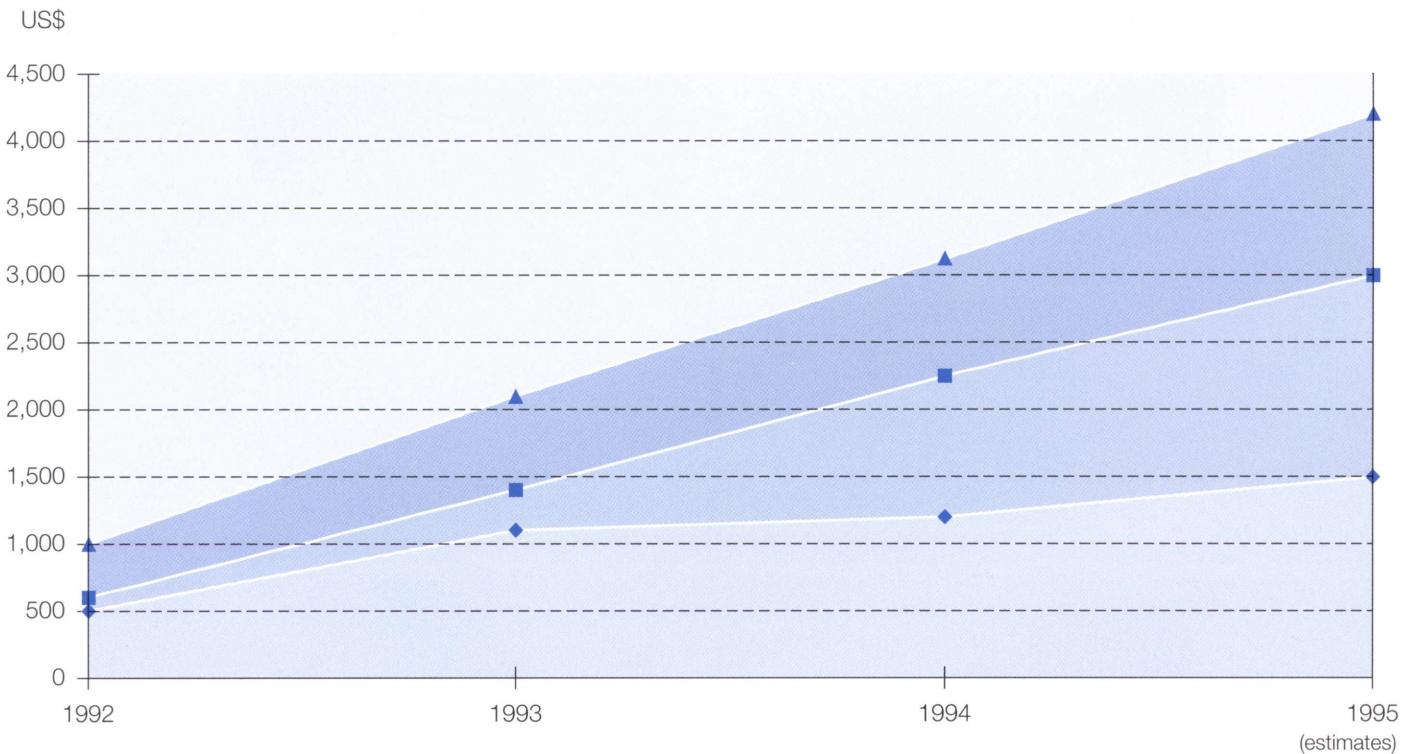
Source: UN/ECOSOC

Foreign portfolio investment amounted to approximately US\$ 700 million, compared to US\$ 500 million of foreign direct investment in the first half of 1995, according to Goskomstat <sup>1</sup>.

The European Union is also the major foreign portfolio investor in Russia. 48.4 per cent of total portfolio inflows came from the Member States of the European Union in the period January to June 1995. Germany (19.7%) is the second biggest single investor behind the United States (27.5%). Japanese investment in Russia only amounts to 3.2 per cent of total portfolio investment in the same period.

Portfolio investors have started to diversify and spread shares among several sectors of industry. According to Goskomstat, 15.2 per cent of total foreign portfolio investment went into chemicals and petrochemicals and 13.5 per cent to fuels in the period January to June 1995. The food industry followed with 12 per cent, retail trade and catering with 10 per cent. Financial and market infrastructure reached 9 per cent, whereas the wood and paper industry attracted 8 per cent of total foreign portfolio investment in the same period.

**Trends in foreign investment in Russia (1992-1995)**



Source: Goskomstat; PlanEcon.

- Foreign direct investment
- Portfolio investment
- Other flows

<sup>1</sup> OECD/CCET



## Investment promotion

The European Union has undertaken several efforts to help promote FDI in the NIS.

Firstly, the European Union has significantly increased its commitment towards the funding of investment support for EU-NIS small and medium-sized enterprise joint ventures and for small-scale infrastructure projects in border areas.

The European Union extended its JOP facility to the NIS in 1996.

The aim of the Joint Venture Programme (JOP) is to facilitate productive European Union investment in the NIS. By encouraging cooperation between partners located in the EU with partners in the NIS, the EU contributes to the efforts of the NIS towards developing productive investment and a market economy. Finance may be provided through a combination of INTERREG, Phare and Tacis to support measures aimed at promoting inter-state, inter-regional and cross-border cooperation, including small infrastructure projects in cross-border areas.

Within the framework of the Tacis nuclear safety programme, the EU has also started to devote a greater share of the budget for investment finance.

In the energy sector, the European Union has tried to provide investment guarantees. Unfortunately, the efforts so far have not led to any significant success.

Last but not least the Partnership and Cooperation Agreements will offer greater security to companies and investors from the EU, and thus encourage the direct investment which is needed by the economies.

Finally, there are plenty of initiatives by the EU Member States to provide instruments which help to promote investment in the NIS.

However, one should keep in mind that the possibilities for investment promotion by the international community are limited. According to surveys among foreign investors, the crucial role for encouraging FDI must be played by the recipient governments themselves. Unless they guarantee a sufficiently stable legal framework and provide for a favourable business climate, foreign investors cannot be persuaded to invest, but are discouraged by uncertainty and high risk.

It is in the interest of the NIS governments to remove trade and investment obstacles and push for a more rapid integration into the world economy. The European Union supports these endeavours in every respect to foster sustainable development in this region.







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