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Comparative Analysis of the Armenian Exports: Eurasian Customs Union vs. Association Agreement

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Abstract

This work examines the potential impact of emerging Eurasian Customs Union on Armenia's economy with special emphasis on the export sector. It scrutinizes how the benefits of Armenian exporters are shifted when the average tariff level of exports is changed as a result of the decision made by the government of Armenia to join the newly emerging Customs Union. It makes comparative analysis of Armenian exports depending on the choice of Armenia to join Customs Union or to sign Association Agreement to find out which scenario was more beneficial for Armenian exporters.

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Abbreviations and acronyms

AA — Association Agreement

CU — Customs Union of Belarus, Kazakhstan and Russia

CET — common external tariffs

CES — common economic space

CGE — computable general equilibrium

CIS — commonwealth of independent states

DCFTA — Deep and Comprehensive Free Trade Area

EaP — Eastern Partnership

ECU — Eurasian Customs Union

ENP — European Neighborhood Policy

EurAsEC — Eurasian Economic Community

FTA — free trade area

FOB — free on board

GDP — gross domestic product

GATT— general agreements on tariffs and trade

GTAP — global trade analysis project

GR — gross revenue

IMF — international monetary fund

MFN — most favored nation

PTA — preferential trade area

RA — republic of Armenia

RTA — regional trade agreements

SES — single economic space

SITC — Standard International Trade Classification

SQ — status quo

UNCTAD — United Nations Conference on Trade and Development

WTO — world trade organization

1. Introduction

Regional trade areas in the form of free trade agreements or customs unions generally have a significant impact on the economy and welfare of the member countries. Thus, countries' decision to become a member of a particular regional trade agreement is not an easy task. This is what put Armenia into an ambiguity to choose between free trade agreement with the European Union and customs union with Russia, Kazakhstan and Belarus.

The process of the negotiations for the establishment of the Eurasian Customs Union dates back to more than 8 years. Almost immediately after the formation of the Eurasian Customs Union in 2009 the common external tariff was introduced. Unlike other regional trade agreements existing in CIS, this Customs Union is a deeper stage of integration with its common import taxation structure, common external tariff and the harmonization of product quality, sanitary and other standards. Currently this is a Union with no internal tariffs for the trade among member countries, with external tariffs with third the countries¹, having far-reaching plans of deep integration, to emerge into Eurasian Economic Union. On September 3, 2013 the President of the Republic of Armenia Serzh Sargsyan in his meeting in Moscow with the President of Russian Federation Vladimir Putin announced Armenia's willingness to join Russian led customs union with the republic of Belarus and Kazakhstan. This announcement immediately got a negative feedback and caused uproar in Armenia. Many scholars claimed that the decision to join Eurasian Customs Union will not promote national economy of Armenia, while DCFTA and Association Agreement with European Union could increase the welfare of the country and boost the economy. Both these regional trade agreements eliminate trade tariffs with Armenia by

¹ Third countries are non-member countries. For instance, in the case of ECU third countries are all other countries trading with Armenia besides Russia, Kazakhstan and Belarus.

promoting more liberal trade between partner countries. However, the major difference between agreements is that customs unions limit country's sovereignty of its trade policies by introducing common external tariffs with third countries. Hence, this study analyzes the potential impact of emerging Eurasian Union on Armenia's economy with special emphasis on export sector. It scrutinizes how the benefits of Armenian exporters are shifted when the average tariff level of exports is changed as a result of the decision made by the government of Armenia to join the newly emerging Customs Union.

Firstly, theoretical reasoning of the regional trade agreements leading to different effects on welfare of the countries is scrutinized. Secondly, it is tested empirically based on sectorial tariff analysis for the exports from Armenia. This work is an attempt to test the following hypotheses:

H1: Maintaining status quo is *significantly* more beneficial for Armenian exporters than joining ECU or signing AA.

H2. Joining Eurasian Customs Union is *significantly* more beneficial for Armenian exporters than maintaining SQ or signing AA.

H3. Signing AA with European Union is *significantly* more beneficial for Armenian exporters than joining ECU or maintaining SQ.

In order to test these hypotheses and to understand which path is more beneficial in line of exports for Armenia the research question "Is Armenia's decision to join Eurasian Customs Union more beneficial for Armenian exporters than signing European Association Agreement" was raised.

Three scenarios corresponding to each hypothesis are discussed in this study. By putting the emphasis on the sectorial analysis of the tariffs, we will examine the change in the revenue of exporters in three different scenarios. The comparison of the sum of net revenues in these scenarios will give an opportunity to record the change in the size of Armenia's total exports and to conclude which path is more beneficial for the exporters. In order to do so, variables such as transportation costs, quantity of the exported goods, prices of the products, composition of the exports and non-tariff barriers are taken as fixed. Possible gains coming from the tariff change when Armenia is in the CU and probable gains that could come from AA are put in relationship with the GDP and total exports of Armenia to examine how big the share of those possible benefits is in these two components.

The article is organized in the following manner. First chapter starts with the literature review on the synthesis of the findings of different authors related to the topic. Both theoretical and empirical analyses are taken into account in the literature review. Second chapter provides background of the establishment of Eurasian Customs Union and emerging process of DCFTA agreement. This chapter also presents the methodology of the study and data collection.

Armenia's export structure by 16 partner countries, 36 product groups and exports in thousands of dollars is analyzed. The next section reconsiders the outcomes and findings of the study taking into account the analysis of three scenarios. Finally, conclusion is followed.

1.1 Literature Review

There is a huge scholarly attention drawn on various types of free trade areas, customs unions and other regional trade agreements signed between different countries. These FTAs, CUs and other trading blocks have been comprehensively studied through the lenses of the literature on regionalism. In economic literature regionalism is not a new topic. It came with two waves, from which second one was more successful in terms of formation of new blocks of countries. The first wave of regionalism was more successful in Western Europe and in 1991 it was called “First Regionalism” by Bhagwati (later in 1998 Ethier called it “Old Regionalism”). The second wave called “New Regionalism” was more notable with the big number of countries involved in regional blocks and it was stated that almost every country is involved in at least one trading block (Mrazova 2010; Freund and Ornelas 2010; Mkrtchyan and Gnutzmann 2013). However, a subtle difference between the customs unions and free trade areas complicates the literature relating the regional trade and marks it by deep ambivalence. Hence, precise definitions for regional trade agreements are important to differentiate them. A Preferential Trade Area (PTA) is “a union between two or more countries in which goods produced within the union are subject to lower trade barriers than the goods produced outside the union” (Panagariya 1998, 2). A Free Trade Area (FTA) is a kind of Preferential Trade Area where “member countries do not impose any trade barriers on goods produced within the union but do so on those produced outside the union” (Panagariya 1998, 2). Finally, a Customs Union (CU) is a union where member countries apply common external tariffs (agreed by all members) on goods imported from non-member countries of the union (Panagariya 1998). Freund and Ornelas (2010) claim that in contrast to FTA member countries, which maintain their external trade policies, CU members create a

common external tariff structure and this peculiarity affects countries' decision and consequently their welfare. FTAs constitute the overwhelming majority of the regional trade agreements and are more common than CUs, while CUs have much larger memberships. According to the 2013 database of WTO from all 250 agreements, which are in force now, about 84% are free trade agreements. Generally FTAs consist of a small number of partner countries, which usually are not so close geographically. FTA member countries are aimed at achieving essential reciprocal and preferential trade liberalization during short period of time, and at the same time preserve their sovereignty when trading with the rest of the world. By contrast, the number of member countries involved in the customs unions is relatively high and often partner countries are near geographically. Here, the process of negotiations lasts longer than in the case of FTAs. Moreover under CUs member countries partly lose their autonomy in international trade (Andriamananjara 2011, Freund and Ornelas 2010). Thus, the need to adjust third party suppliers' tariffs is the key difference between CUs and FTAs which affect countries preferences to choose between CUs, FTAs or no agreement. Hence, the questions which are generally raised in existing literature are 1) whether all these regional agreements make countries, as well as the world better off and 2) which one is more preferable for the countries: FTAs, CUs or no agreement.

As an answer to the first question Viner (1950), Mrazova (2010) and Freund and Ornelas (2010) claim that customs unions or FTAs not always lead to the increase in welfare of the member countries or outsiders. The trade diversion is the major reason of this. This diversion on its turn is a consequence of the preferential removal of tariffs where more efficient non-member suppliers are replaced by less efficient once of partner countries. It generates inefficiency and shortcomings in the world production and especially harms countries outside the block (Viner

1950; Mrazova 2010; Freund and Ornelas 2010; Andriamananjara 2011). Thus, CUs and FTAs are tended to be welfare reducing when trade diversion dominates creation.

In academic literature central analysis relating the trade creation and trade diversion state that trade creation increases countries welfare, while trade diversion is welfare-reducing. Trade creation occurs when a product of domestic production is replaced by a low cost good produced in partner country, because in this case producing particular product at home is more expensive than its importation. By contrast, trade diversion is the scenario when member country replaces low-cost products imported from the rest of the world with the higher cost production of partner countries (Krueger 1995). Besides the trade creation and trade diversion framework, tariff changes also crucially affect the welfare of the countries. FTA and MFN external tariffs maximize neither government objectives nor members' social welfare, and this supports to the claim that free trade areas are not Pareto efficient bilateral agreements (Mkrtchyan and Gnutzmann 2013). According to Krueger, FTAs do not generate more welfare benefits than customs unions do, but instead they can create additional welfare costs which are zero under custom unions. By supporting the idea that FTAs can be Pareto inefficient agreements he claims that if all other factors are taken equal, "customs union arrangements are strictly Pareto superior to free trade agreements" (Krueger 1995, 4).

What refers particularly to the CUs, based on a range of models such as Kennan and Riezman (1990) and Ornelas (2007) it was shown that tariff changes under CUs make external tariffs higher than in FTAs (Gnutzmann and Mkrtchyan,II 2013). CU's net economic impact essentially depends on "how the adjustment of external tariff affects the degree of discrimination vis-à-vis nonmember countries" (Andriamananjara 2011, 114). Kemp and Wan (1976) observed welfare enhancing scenario of CUs by showing that if common external tariff of CUs is chosen the way

that trade with the non-member countries and the rest of the world is kept static, then the establishment of the CU can maximize the welfare of all parties and also non-members, contingent on general transfers. Hence, adoption of generally accepted and well-designed CET is the prerequisite for the stability and sustainability of the customs unions (Andriamananjara 2011). There are no many theoretical generalizations relating welfare effects of CUs, but the existing literature largely accepts that if the share of the trade among union partners is larger, it is more likely to have more trade creation and less trade diversion. At the same time, the formation of CUs can be welfare-increasing, when (1) the preexisting tariffs of the member countries are very high, so that it lowers the probability of trade to divert, or (2) very low, the way that lowers the costs of trade diversion (Krueger 1995, Ornelas 2007). Moreover, by contributing to the expansion of the theoretical literature on welfare effects of CUs and FTAs, Salvatore (2007) pointed out several factors affecting trade creation and trade diversion effects of CUs. According to him “larger union size, higher pre-union tariff structure between members, lower pre union tariff structure between members and nonmembers, higher pre-union intra-regional trade, greater substitutability of production structures between members and nonmembers, and geographical proximity will all create larger trade gains” (as was cited in Park 2008, p 9),

Another theoretical generalization concerning CUs and FTAs in the political economy is that adoption of the FTA between two or more countries is inherently more trade diverting than engagement in the customs unions (Krueger 1995; Andriamananjara 2011; Mkrtchyan and Gnutzmann 2013).

The theoretical literature on formation of customs unions and free trade agreements continues to expand, while empirical literature in support of the regionalism theory is relatively scarce and is not growing as rapidly as theoretical studies. When scrutinizing trading blocks and their gains

from liberated trade in empirical analysis much attention is drawn to the factors such as the internal and external conflicts of the countries, non-tariff barriers, membership in World Trade Organization and rules of General Agreements on Tariffs and Trade (GATT now The World Trade Organization). According to definition of GATT article XXIV a customs union is an agreement among its member countries for elimination trade barriers via setting common external tariffs on trade with non-member countries where these common tariffs on average should not be higher than the average of former constituent countries (Konishi, Kowalczyk and Sjöström 2007). Thus, these unions do not impose any tariffs on the goods traded among member countries, but instead charge taxes on goods traded with the rest of the world. Based on this definition one of the world's largest and most successful customs union, the European Union was established in 1958. It started as a common market, based on the Treaty of Rome, by setting its common external tariffs and ensuring free mobility of goods between members (Mkrtchyan and Gnutzmann 2013; Krueger 1995).

Magee and Lee (2001) and Krueger (1995) claim that initial tariffs of this customs union were the counted average of the national tariffs of the members. Under this single market, external tariffs were reduced and non-tariff barriers were dismantled among member countries. This union is also empirical evidence of the claim that customs unions can foster trust between member countries and reduce the risk of the conflicts in the region (Andriamananjara 2011).

Besides Europe, preferential trade agreements, especially FTAs are widespread in East Asia. In this region as of September 2008, about 26 regional trade agreements were adopted. Park (2008) and Andresen (2004) based on the welfare enhancing factors of the CUs made empirical analysis of the East Asian preferential trade agreements, and suggest that from all types of the RTAs the CUs in East Asia are more likely to produce positive stable welfare effects (Park 2008).

Harvie, Lee (2002) and Plummer (2006) discuss particularly the case of Association of South-East Asian Nations (ASEAN) and claim that there will be more gains and economic efficiency when ASEAN customs union with its single market be created.

Harrison, et al. (2001), Sulequl (2003), Romalis (2005) and Frankel (1997) found significant economic effects referring to the welfare of the other preferential trading blocs as North American Free Trade Agreement (NAFTA) and Mercosur. Moreover, Harrison et al. claims that much importance should be given to the improved market access in free trade areas, because when taken bilaterally “trade diversion costs do indeed dominate the welfare effects of these agreements unless sufficient market access is obtained in partner countries (or third country tariffs are lowered)” (Harrison et al., 2001, p. 2). Sulequl and Romalis find out that these regional agreements have substantial effect on international trade even without providing sufficient market access. Romalis analyzed the impact of these agreements on international trade grounded on world-wide trade data for almost 5000 commodities. Sulequl based on quantitative indicators of trade creation and trade diversion argued that mature regional trade agreements such as NAFTA and EU in general improved the economic welfare of both member and non-member countries.

Park (2008), Magee (2008) and Baier and Bergstrand (2007) analyzed the effects of RTAs based on the well-known gravity regression model. According to them the analysis of the ex-post effects of the RTAs on international trade and trade between members essentially depends on the type of the RTA. Particularly Magee’s estimates pointed that “Customs Unions generate the largest long-run increase in intra-bloc trade on average, with free trade agreements having smaller long-run effects” (Magee 2008, 21). The key findings of these analysis was that generally the long-run effects of the RTAs are more positive than short-run effects.

The literature referring particularly to the Association agreement of the EU and analysis of the tariff change under Customs Union is relatively scarce. The quantitative analysis of Haddoud, et al. (2013) based on the model of Lloyd and Maclaren (2004) were for the assessment of the EU's Association Agreement's impact on the trade of Albania. Their calculations of the volume of imports from the EU and non EU member countries indicated that European Association Agreement increased Algeria's trade with both EU and non-EU countries during the first four years of the implementing agreement. While this pattern was changed after four years, and the future effect of the agreement was negative as trade changes with EU and non-EU countries were about -\$2.7 billion.

Nasser Saidi (1996) and UNEP report (2005) assessed the impact of EU-Lebanon partnership agreement on the trade of Lebanon, with the focus on export sector and found out that the agreement is of strategic importance. UNEP report's primary focus was on impact of EU's Association Agreement on the exports of olive oil sector of Lebanon where two scenarios were elaborated for the assessment of the trade changes. The findings of the assessment was that even the agreement is welfare enhancing for Lebanon, there is a need to implement a set of regulatory improvements that will improve oil sector export up to European standards.

Much work has been done in assessment of tariff changes of EU Association Agreement with the Chile, Central America and Eastern European countries. Chritophe Rault et al., (2007) and Itaq Sarl (2012) found out that from the economic point of view the effect of regionalism and particularly the Association Agreement of EU had a positive but moderate impact on exports of Chile and East European countries. Fernando R. Junquera (2009) and ECORYS report on "Trade Sustainability Impact Assessment of the Association Agreement to be negotiated between the EU and Central America" (2009) claim that the effect of the agreement will be significant if the

countries deepen their bi-regional relations. More specifically ECPRYS report based on the results of the computable general equilibrium model found that the deeper is the integration of EU and Central American countries, the more beneficial the effects will be in the long run. Jensen and Tarr (2011) also find the same results but in the case of Armenia and EU association agreement. They claim that there will be substantial gains for Armenia from DCFTA but only in the case when they deepen the agreement and their cooperation.

Isakova and Plekhanov (2012) and World Banks Report on “Assessment of Costs and Benefits of Customs Union for Kazakhstan” (2012) analyzed tariff change under Customs Union particularly on the trade of Kazakhstan. The empirical results of these studies suggest that tariff change bring some trade diversion in Kazakhstan and that the rise of average level of tariffs is tended to reduce real income of Kazakstan by more than 0.2% of consumption.

Mkrtchyan and Gnutzmann (2013) and EDB’s report on “Armenia and the Customs Union: Impact of Economic Integration” (2013) assessed CU integration effect on trade and GDP dynamics of countries based on the multiple regression model of trade. According to their estimations CU increases tariff levels above the weighted average in member countries. The estimations of EDB’s report indicated that Armenia will gain many advantages from integration with the CU-SES, but these advantages largely depend on “successful solution of the key problems: transport; energy; railway and motorway export via Georgia; labor migration legalization and the absence of restrictions...” (Eurasian Development Bank 2013, p. 8).

The literature review revealed some factors affecting trade diversion and trade creation of the trading blocks, and the effects of regional trade agreements, but the case of Armenia still remains less scrutinized. Armenia’s decision to join Eurasian Customs Union instead of Association

Agreement is a recent case, and this is newly developing topic in literature. Although we can find some analysis referring to Armenia in the AA and Armenia joining to CU but there is no work done analyzing both cases together.

Thus, this study contributes to the existing literature by analyzing and comparing the effects of both agreements by a special focus on export sector. Based on the quantitative analysis done in this work, it was found that both AA and CU cases are more beneficial for Armenian exporters than preserving status quo. When the gains of the Customs Union and Association agreements are compared, for Armenian exporters the revenues raise more significantly when Armenia chooses to be in the second CU scenario. All findings indicate that gains coming from Eurasian Customs Union of Russia, Kazakhstan and Belarus are more than the benefits of AA. The share of those benefits in the GDP of Armenia again is more visible than the gains of AA, but in this case these benefits do not affect the GDP or total exports significantly.

1.2 Short Overview of the Armenia's Economic Choice: CU vs. AA

Armenia in the Eurasian Customs Union

Almost ten years have passed since the South Caucasian region (Armenia, Georgia and Azerbaijan) was included in the European Neighborhood Policy (ENP). Continuous progress in relations with the partner countries reached to the stage of signing Eastern Partnership which was adopted by the Union in spring 2008. This was a policy questioned by some authors as being geopolitical challenge to Russia's domination (Sergunin 2013; Nixey 2012; Avedian 2013; De

Wilde and Pellon 2006). Two years later on January 2010 the Customs Union between Kazakhstan, Belarus and Russia came into force. Armenia being a candidate for Deep and Comprehensive Free Trade Agreement (DCFTA) initiated by European Union was offered to join newly emerging Eurasian Customs Union. This put Armenia into the ambiguity to choose a regional trade policy either with developing countries or with already developed ones (Jensen and Tarr 2011).

The process of the negotiations for the establishment of the Eurasian Customs Union dates back more than 8 years. In August 2006 during the informal summit meeting of EurAsEC the first step for establishment of Customs Union was done, with future plans that Kyrgyzstan and Tajikistan will join to the Union in the nearest future (Eurasian Economic Commission 2013). On 6 October 2007 the presidents of Kazakhstan, Belarus and Russia signed the Treaty Establishing the Customs Union (Wolffgang et al., 2012). After the hit of the global financial crisis of 2008 members accelerated the process of integration as a way for minimizing economic risks. Already on January 1, 2010 the Single Economic Space on the basis of the Customs Union was launched (Eurasian Economic Commission 2013). This Union bears a significant economic weight as a result of large population size of the member countries which enlarges the consumer market and about US\$900 billion goods turnover (Carneiro 2013). The annual GDP of the Union exceeds US\$2 trn., where Russia's share is 86% of the block's GDP and 84% of the population. The share of Kazakhstan and Belarus is quite small: 8% of GDP and 10% of population for Kazakhstan, and about 5% for both population and GDP for Belarus (Mkrtchyan and Gnutzmann 2013). Almost immediately after the formation of the Eurasian Customs Union the common external tariff was introduced with about 80% coincidence with the Russia's import duties (Wisniewska 2012). Unlike other regional trade agreements existing in CIS, this Customs Union

is a deeper stage of integration as it is not only free trade among member countries but also introduces a “common import taxation structure and common external tariff, as well as the harmonization of product quality, sanitary and other standards” (Kasciunas and Sukyte 2013, 64).

One year later in June 2011 internal customs controls were abolished in the Union. Currently this is a Union with no internal tariffs for the trade among member countries, with external tariffs with third countries and far-reaching plans of deep integration: emerging into Eurasian Economic Union (Mkrtchyan and Gnutzmann 2013). Common Economic Space started functioning on 1 January 2012; however because of disagreement in implementing different principles and acts the shift to the Common Economic Space was postponed to 2015. The principles of this economic space indicate that Kazakhstan, Russia and Belarus plan to “harmonize their economic policies, including: agreeing on uniform principles of access to the services of natural monopolies, standardization of the competition policy, and harmonization of the services market” (Wisniewska 2012, 2). The harmonization of the transport, energy and monetary policies and the free movement of labor and capital also are involved in the framework of Common Economic Space (Wisniewska 2012). Currently Union aims at extending membership by involving Kyrgyzstan, Ukraine and Armenia in the Union. The negotiations of Kyrgyzstan membership started in late 2011. While, with Armenia and Ukraine the negotiation’s process started one year later (The World Bank Report 2012). In the framework of the CES, countries succeeded only to ensure the free movement of labor. Workers of the three countries are not obliged to apply special work permits and under the CES they should be treated as nationals. While, in the case of the free movement of goods Union still have many gaps (Wisniewska 2012). The key area where three member countries are trying to deepen integration is in the trade

facilitation. In this field the intention of the countries is to reduce the cost of the trade between them by decreasing the number of required documents and making easy to obtain them. The reduction of the non-tariff barriers is in the scope of the deep integration of the countries (The World Bank Report 2012). Although countries succeeded to eliminate all trade tariffs among member countries, non-tariff barriers hampering the trade still exist in the Union (Wisniewska 2012). Sanitary and phyto-sanitary measures and other technical regulations are considered to be essential cost-increasing barriers for the exporters. Under this customs union the governments of the member countries are implementing programs aimed at harmonizing technical regulations and introducing agreements of mutual recognition, although, there is no significant progress in this sector (The World Bank Report 2012).

The immediate impact of the Custom Union on members was an increase in the external tariff in many sectors in Kazakhstan and relatively few other sectors for Belarus and Russia (Mkrtchyan and Gnutzmann 2013; Dreyer and Popescu 2014). Kazakhstan which had the most liberal trade before the CU faces an increase in import tariffs where an average applied rate almost doubled from 6.5% to 12.1% (Dreyer and Popescu 2014). However, internal trade grew in the following years after the establishment of the CU. By 2011 intra-CU trade share among member countries rose by 17% compared with the 2009. In the years before the establishment of the Union the amount of the internal trade between three countries was about US\$44bn., which grew and reached to US\$62bn. by 2011. Belarus and Kazakhstan exports to Russia amounted for 18% and 10% of the total, while in 2011 this amount more than doubled (Mkrtchyan and Gnutzmann 2013).

The ambitions of the Eurasian Union to transform into “Single Economic Space” and already in 2015 to the “Eurasian Economic Union” forces to think that this is not pure economic project but

also political. The expansion of the Union starts from the point of involving Kyrgyzstan, Armenia, Moldova and Ukraine in the Union. On September 3, 2013 President of the Republic of Armenia Serzh Sargsyan during his meeting in Moscow with the Russia's President Vladimir Putin declared that Armenia is going to join Russian led customs union with the republic of Belarus and Kazakhstan (Emerson and Kostanyan 2013).

Vilnius summit: Armenia did not initiate AA

After involvement of the South Caucasus into the European Neighborhood Policy (ENP), EU's next step was deepening the integration process of the region and involvement in the Eastern Partnership. The aim of ENP was setting ambitious objectives for partner countries for making political, institutional and economic reforms, enhancing cross border cooperation and sharing responsibility in conflict prevention and resolution. In other words, this is considered something meaning more than a partnership and less than a full membership (De Wilde and Pellon 2006). In the framework of ENP and Eastern Partnership European Union supported Armenia in different ways: financial support, promotion of international order and European values, standards and deeper integration both politically and economically into global and EU markets. Moreover, limited financial aid, promotion and development of different institutions can be the best answer to the question what EU has done to help Armenia so far. The central goal of EU-Armenia cooperation is to develop an essentially close relationship between Armenia and the EU, going beyond the past stages of cooperation to the further deepening economic and political cooperation by stimulating economic growth and poverty reduction projects (Caucasian Institute for Economic and Social Research 2013; Navasardian 2011). Armenia has made a progress in many areas of the Action Plan of the ENP which made the political and economic systems closer

to the European standards (Navasardian 2011). In 2009 European Council for undermining the impact of the global crisis on Armenia's economy provided EUR 65 million loan as a financial assistance and a grant of EUR 35 million (Babayan 2011). Armenia together with Moldova, Georgia and Ukraine has been targeted by the EU to be involved in "Deep and Free Trade Area" (Jensen & Tarr 2011).

Under the Eastern Partnership EU-Armenia Association Agreement (AA) negotiations have a big progress. These negotiations with Armenia began in July 2010 as a new project replacing the old "Partnership and Cooperation Agreement". More deeply negotiations on the trade sector were launched in May 2012 by the name of "Deep and Comprehensive Free Trade Area" (European Commission 2013). Especially there was a big progress in the sector of implementing the key recommendations for the initiating negotiations for a Deep and Comprehensive Free Trade Area. One of those preconditions was becoming a member in the World Trade Organization (WTO) which Azerbaijan, for instance, by being partner country of the ENP refused to implement (Caucasian Institute for Economic and Social Research 2013). From the cooperation with the EU Armenia enjoys official, political and public support, and every sector of Armenia's sociopolitical arena have its interests and incentives. This refers to the executive and legislative bodies, opposition party and the civil society (Navasardian 2011). Besides this kind of assistance, European Union Under the Eastern Partnership Comprehensive Institution Building project provided EUR 32 million to the Armenia in support of the "Deep and Comprehensive Free Trade Area" (DCFTA) negotiations from 2011-2013, and also EUR 22 million to promote and improve the reforms in public finance management and transparency in public sector related to the DCFTA (European Commission 2012). Thus, the dilemma for Armenia is whether or not the EU will continue to support her financially as a neighborhood member after Armenia's decision not

to sign Association Agreement with the Union. The second question which rises for Armenia is whether the choice of Customs Union both economically and politically beneficial for the country. One of the noteworthy facts here is that Armenia also should take into account Georgia's choice of integration into European or Eurasian Union. Moreover Georgia signed DCFTA agreement which made that country to be one step closer to the European Union.

The negotiations on Deep and Comprehensive Free Trade Area with Georgia launched in December 2011, while with Armenia it started one year later in February 2012. This agreement gives to the partner countries an opportunity of economic integration and benefits which contributed to the rapid development of western economies. They gain an access to modern and sophisticated technology which is necessary for modernization and development. DCFTA also brings benefits from the EU's investments (Sergunin 2013; Caucasian Institute for Economic and Social Research 2013). Armenia has been on track to initiate AA in the Eastern Partnership summit in the Vilnius which had not occurred because of the unexpected announcement of the president of the RA instead to join the Russian-led Customs Union. This third Eastern Partnership summit took place on November 28-29 2013 in Vilnius in the capital of Lithuania. The heads of the six partner countries governments: Armenia, Azerbaijan, Georgia, Belarus, Ukraine and Moldova, and their representatives have met with the representatives of the Union and member countries. The objective of the summit was evaluating the progress of the partner countries and welcoming the steps to strengthen the Eastern Partnership since the previous summit in Warsaw. Building a common area of shared democracy, stability, prosperity and increased level of interactions were the key priorities of the projects discussed during the summit (European Parliament/Audiovisual Services for Media 2013).

As two unions are incompatible due to their different customs policies, Armenia's choice precluded any farther trade integration in the framework of Association Agreement. Although, it was stated that EU will continue to support Armenia and that they will "further develop and strengthen their cooperation in all areas of mutual interest within the Eastern Partnership framework, stressing the importance of reviewing and updating the existing basis of their relations" (European Parliament 2013, 2). The summit participant countries in the framework of the European Neighborhood Policy and the Eastern partnership, confirm that they have sovereign right to freely choose the level of ambition and purposes to which they aspire in the cooperation with the European Union (European Parliament/Audiovisual Services for Media 2013). Also summit participants and the high representatives of the EU welcomed the launch and entry into force of the Framework Participation Agreement (FPA) with Moldova and Georgia and their interests in being engaged in EU operations. It was mentioned that the launching of the negotiations with Armenia, Ukraine, Azerbaijan and Belarus is under construction (European Parliament 2013; European Parliament/Audiovisual Services for Media 2013).

Armenia's choice to join Customs Union instead of Deep and Comprehensive Area of the EU became the reason of grievances of society and some public officials particularly from opposition parties. They were mainly angry about the fact that this kind of crucial decision was mad without any public consultations or debates in parliament. When Kremlin initiated the formation of the Eurasian Union for which inclusion into the customs union was the first prerequisite Russia firstly attempted to involve countries of the Commonwealth of Independent States. Hillary Clinton considered it as a Russia's efforts for re-Soveitization of the former Soviet Union countries. She claimed that US knows about Russia's intentions to dominate former Soviet Countries by extended regional integration called Customs Union or Eurasian Union and

mentioned that US is intended to slow down or prevent it (Clinton vows to thwart new Soviet Union 2012). Starting from this point, the representatives of the EU and some senior officials repeatedly and officially warned partner countries of the EaP that joining to the customs union and Kremlin-led Eurasian Union is not compatible with the Association Agreement and integration into the DCFTA (Caucasian Institute for Economic and Social Research 2013).

Thus, Armenia's unambiguous choice also was incompatible with the prospect of the Association Agreement and this became a reason of scrapping Association Agreement with the EU (Popescu 2013). High Representative for Security Policy and Foreign Affairs of European Union Maja Kocijancic claimed that in the case that Armenia joins any customs union, "this would not be compatible with concluding a bilateral Deep and Comprehensive Free Trade Agreement between the European Union and Armenia" (as cited in Caucasian Institute for Economic and Social Research 2013, 172). She also explained that because of the common external tariff trade policy of the customs union, partner countries no longer have independent and sovereign control on their external-trade policies and this is why it becomes impossible to be a member of both unions in the same time (Caucasian Institute for Economic and Social Research 2013). Romas Svedas considers this all a case of geopolitics and stresses that Armenia's decision to join customs union was because of Russia's fight for domination and Armenia's dependency upon Russia (EU-Russia rivalry looms over Vilnius summit 2013). Ukrainian former Prime Minister Anatoliy Kinakh also focused on geopolitics, by mentioning that the geopolitical situation of Armenia explains its choice of Customs Union. He stated that such factors as complex geographic location of Armenia, the unsolved question of Karabakh and Armenia's access to the outside markets and world can explain the decision of the president Sargsyan. Many public officials and political analysts stressed that countries of the Eastern Partnership ultimately want

to be part of the European Union, but Russia's dominance does not let them. Particularly for Armenia it was mentioned that Armenian government would like to sign the Association Agreement with the EU, but its main concern is security issue. According to them² the arms trade of Russia with Azerbaijan also was a mean to put pressure on Armenia to implement Moscow's aim (News Analysis: Armenia's Choice Stirs Competition Between Moscow, EU 2013).

On the other side some of Armenian public officials and scholars claimed that Eurasian Union neither economically nor politically is beneficial for Armenia. Richard Giragosyan also put the stress on the pressure from the Russian side and stated that the only benefit from the Eurasian Integration can be minor development of the resolution of Karabakh conflict, but that development will have no tangible changes. At the same time, Stepan Saparyan, the opposition Heritage Party's Secretary General noted that Armenia should have good relations with Russia but should not join the customs union as it is not beneficial for Armenia at all. He added that Eastern Partnership program is challenging Russia's influence and this is realistic perspective, while Eurasian Union is still only on paper. The fact that Armenia has no common border with Russia and that trade is possible only via Georgian routes was a basis for his claim that Customs Union will not give anything to the country (Armenia should not join Eurasian Union, opposition says 2012, Expert: Russia will try to urge Armenia into Eurasian Union 2012). Other officials and analysts (Paruyr Hayrikyan, Ara Papyan) argued that Armenia should know for sure that joining the Eurasian Union will harm its relations with the European Union and Middle East, and as it has no benefits from Eurasian Union there is no reason to join it (Armenia Doesn't Need It 2012). Paruyr Hayrikyan opinion was more radical towards integration into Eurasian Union. He

² Amanda Paul, "News Analysis: Armenia's Choice Stirs Competition Between Moscow, EU 2013", EU-Russia rivalry looms over Vilnius summit 2013. The words of the member of European Parliament's Foreign Affairs Committee Charles Tannock also are noteworthy, as he put the stress on Moscow's pressure on Armenia taking into account the security issues which country has nowadays.

claimed that joining customs union means nothing but 100% collapse of the economy and doubled number of the migration level. He stated that already 20 years Armenia did everything to be a step closer to the EU but this decision puts an end to their relations (P.Hayrikyan about CU 2013).

Sudden decision of the president of the Republic of Armenia to join Customs Union became a reason for riots in the country. The dilemma for Armenia whether to deepen the integration with European Union or with the Eurasian Union was solved in favor of Russia. Today Armenia is in the stage of elaborating a roadmap for entry. The next step will be to adopt international legal document envisaging Armenia's participation directly in the process of Eurasian integration.

2. Methodology and Data Analysis

Numerous articles have analyzed the economic effects of the regional trade agreements (RTAs) on the world trade and welfare of the member countries. The impact of these RTAs was assessed based on models such as computable general equilibrium (CGE), Global Trade Analysis Project (GTAP), gravity equation and etc. In contrast with these previous studies, this study examines RTAs possible impact not on countries' welfare as a whole but particularly on the size of exports, and consequently on the net revenues of exporters. Depending on the decision of Armenia to choose between Association Agreement with European Union and Eurasian Customs Union with Kazakhstan, Belarus and Russia, the export patterns will be changed significantly due to the changes in tariffs.

The question that arises here is why the focus of the study is on the shift in exports and not in imports. Assessing how increase or decrease in tariffs after joining CU or signing FTA can affect

the size of exports from Armenia, the net change in the revenue of Armenian exporters can be measured, which is not the case when the import change is under scrutiny. When tariffs' impact on the import size is assessed, there is a problem of redistribution of the revenues that government gains as a result of increased external tariffs. In other words, when tariffs on the imported goods are raised, the revenues coming from those tariffs can be redistributed the way that society gains more than before the tariff change. And the opposite also is a case: depending on the redistribution schemes of the politico-economic institutions, price shifts in imported goods can be good or bad for the society. Thus, assessing the impact of tariff change on imports is very complicated when there is no information about government policies referring to the redistribution of the gains of increased tariffs. While, in case of exports the changes in external politico-economic institutions are less likely which gives the opportunity to measure how exports will be changed. When Armenian firms export goods from Armenia and are obliged to pay higher tariffs in the countries importing goods, because of joining CU or adopting AA, then our exporters will have losses which are measurable.

Export has direct positive relationship with GDP, and is one of the important components of it. GDP is the sum of 4 components: consumption, investment, government purchases and net exports. Each dollar of GDP is in one of these components. In this analysis of Armenian exports, the stress is put on two points, that 1) Armenia is a small open economy, which exports goods and services abroad, imports goods and services from abroad and borrows and lends in world financial markets, and 2) it is perfectly competitive market, and is price taker rather than price setter. In small open economies such as Armenia, international trade is central to analyzing economic developments of the countries, hence, the role of exports should not be ignored

(Menkiw 2011). The increase in exports will bring an increase in GDP, but in the case of the imports the relationship is negative.

All these factors taken together explain why so much importance is given to the assessment of the changes in exports. Hence, when all other factors are taken constant, the change in exports as a result of tariff change can show whether Armenian exporters benefit from joining CU or from signing DCFTA.

2.1 Methodology

The aim of this study is to estimate the impact of the removal of tariffs on Armenian exports, depending on its decision to join CU or sign DCFTA. In order to do that, we take as fixed all other variables such as transportation costs, quantity of the exported goods, prices of the products, composition of the exports and non-tariff barriers. Armenia's export structure by 16 partner countries, 36 product groups and exports in thousands of dollars is analyzed. In 16 partner countries 7 are member countries of the European Union: Germany, Belgium, Sweden, Italy, France, Netherlands and Bulgaria, 3 member countries of the Customs Union: Kazakhstan, Russian Federation and Belarus, 2 neighboring countries Georgia and Iran, and the remaining are the other 3 trade partner countries: Ukraine, USA, Canada and China.

Three scenarios are elaborated for understanding which path is more beneficial in line of exports for Armenia. The first scenario is the status quo of Armenia, when it decides neither to join CU, nor sign the DCFTA. In this case we count gross revenue of the exporters based on the tariffs

that they are paying currently. Here the profit margin of exporters is fixed as 20% ($\pi=20\%$).

Hence, the formula of the gross revenue is the following:

$$GR = FOB_{value} * (1 + t_1) * (1 + \pi)$$

where GR is gross revenue, which at the same time shows the multiplication of final price with the quantity of the exported product, FOB (free on board) is the total value of the exported product on the board (not a unit cost, but all the exported quantity of the product), where tariffs and the revenue of exporters are not counted, t_1 is the tariffs imposed on goods in the status quo, and $\pi=20\%$ is the fixed profit margin value.

Gross revenue at the same time shows the market price of the product: it includes production cost of the good, imposed tariff in the border, transportation and other fixed costs and the X revenue of the exporter. This is the price by which good is sold out. Thus, in status quo (SQ) Armenian exporter's gross revenue will be FOB_{value} multiplied by the tariff of status quo and multiplied by her/his revenue. While, in when the scenario changes and Armenia joins Customs Union the tariffs and consequently the revenue of the exporters will be changed:

$$GR_{SQ} = FOB_{value} * (1 + t_1) * (1 + \pi_1)$$

$$GR_{CU} = FOB_{value} * (1 + t_2) * (1 + \pi_2)$$

In the second scenario t_2 and π_2 are new tariff and profit margin respectively when Armenia joins the CU. As the market price is taken as fixed, and the production cost also is fixed then $GR_{(SQ)} = GR_{(CU)}$, and FOB is constant. All this factors taken into account we get this equation:

$$FOB_{value} * (1 + t_2) * (1 + \pi_2) = FOB_{value} * (1 + t_1) * (1 + \pi_1)$$

$$(1 + t_2) * (1 + \pi_2) = (1 + t_1) * (1 + \pi_1)$$

$$\frac{1 + t_1}{1 + t_2} = \frac{1 + \pi_2}{1 + \pi_1}$$

This ratio of the tariffs shows how the revenue of the exporters is changed as a result of joining the customs union or signing Association agreement. In case when t_2 (changed tariff) rises the fraction will show how the π_2 decreases, and the opposite. Thus the rate of tariff change is the indicator of revenue change and in the case when the fraction $\frac{1+t_1}{1+t_2}$ is below 1, then t_2 rises, as a result of which π_2 decreases.

Hence, for having more visible picture of the effect of tariff change, we are using the following formulas for three scenarios:

$$NR_2 = \frac{FOB_{value} * (1 + t_1) * (1 + \pi)}{1 + t_1} * \frac{1 + t_1}{1 + t_2}$$

where NR_2 stands for net revenue.

The first scenario analyzed in this study is when Armenia maintains its status quo and current tariffs without joining any regional trade agreement. The sum of the net revenues for each products are compared with the numbers of two other scenarios for seeing which one is more beneficial for Armenian exporters.

The second scenario is the case when Armenia joins the Eurasian Customs Union of Russia, Kazakhstan and Belarus. In this case Armenia will take common external tariffs of the CU, but instead all tariffs among member countries will be eliminated. Hence, here the fraction $\frac{1+t_1}{1+t_2}$ can

clearly indicate how tariff change affected the revenues of the exporters. This scenario again will be compared with the two scenarios of SQ and DCFTA.

Third case is when Armenia decides to sign Deep and Comprehensive Free Trade Agreement. Again as in the previous case there will be tariff change for the exported goods, and tariffs among EU countries and Armenia will be eliminated. Here Armenia can benefit from 0 tariffs with EU but instead can have loses as a result of paying higher tariffs in Russia, Kazakhstan and Belarus. Hence, 3 questions are raised for these scenarios:

- 1) Is maintaining status quo more beneficial for Armenian exporters than joining CU or AA?
- 2) Is joining European Association Agreement more beneficial for Armenian exporter than in CU or SQ?
- 3) Is joining Eurasian Customs Union more beneficial for Armenian exporters than maintain SQ or signing AA?

Based on the fraction of the tariffs, we will see the change in the revenue of exporters, while, comparison of the sum of net revenues in 3 scenarios will give an opportunity to see the change in the size of Armenia's exports and to decide which path is more beneficial for the exporters. This will be done based on calculation of the net wealth, profit margin and rough check. In the analysis net wealth is the difference between sum of the net revenues of the exporters in particular country when Armenia is in the SQ, AA and CU scenarios. For instance, if export in Russia is taken into account, net wealth of Armenian exporters importing in Russia for AA and CU cases will be the following:

$$NW^{Russia} = \sum_{i=1}^N NR_i^{CU} - \sum_{i=1}^N NR_i^{SQ} = \sum_{i=1}^N (NR_i^{CU} - NR_i^{SQ})$$

where, NW^{Russia} stands for the net wealth coming from Russia and N for 16 countries included in the analysis.

In this CU scenario we count the difference between the revenues coming from exporting goods with CU tariffs and goods with current tariffs. The net wealth for the AA scenario will have the following equation:

$$NW^{Russia} = \sum_{i=1}^N NR_i^{AA} - \sum_{i=1}^N NR_i^{SQ} = \sum_{i=1}^N (NR_i^{AA} - NR_i^{SQ})$$

The net benefit ratio (BR) will show the ratio of the sums of net revenues of different scenarios.

Again on Russia's example when Armenia joins CU the benefit ratio will be the ratio of the sum of net revenues of CU scenario and the sum of net revenues of SQ condition. Thus, if the fraction is higher than 1, this means that CU scenario is beneficial for the export firms of RA.

$$BR = \frac{\sum_{i=1}^N NR_i^{CU}}{\sum_{i=1}^N NR_i^{SQ}}$$

If $BR < 1$ then Armenian exporters will have loses in the CU scenario,

$BR > 1$ then CU scenario will be beneficial for exporters.

The formula used for calculation of the profit margin is the following:

$$Profit\ Margin = \left(\frac{\sum_{k=0}^n net\ revenues_{(AA\ or\ CU)}}{FOB_{(particular\ country)}} - 1 \right) * 100$$

The possible gains coming from CU and probable gains that could come from AA are put in relationship with Armenian GDP and exports. The ratios built between these indicators will show how big the share of those possible benefits in the GDP and exports of Armenia is. These will be done based on the following fractions, where Y stands for GDP of Armenia (2012) and E for absolute value of export:

- 1) $\frac{Gain_{SQ}^{CU}}{E}$; $\frac{Gain_{SQ}^{CU}}{Y}$, for CU gains
- 2) $\frac{Gain_{SQ}^{AA}}{E}$; $\frac{Gain_{SQ}^{AA}}{Y}$, for AA gains
- 3) $\frac{Gain_{CU}^{AA}}{E}$; $\frac{Gain_{CU}^{AA}}{Y}$, for comparing 2 cases.

This is one more way to find how big is the impact of that benefits in exports, GDP and consequently on economy of Armenia. Comparisons are done not only by absolute values but also by percentages.

2.2 Data Description

In data collection much emphasis was put on FOB values and tariff data. Exported products involved in the analyses are obtained from Armstat data (only the most exported 36 product

groups were involved). Regarding trade volumes, key focus is on Armenia's exports to partner countries. This data was obtained from UNCTAD data source, which involves the value of total exports and imports of intra-trade of regional and trade groups expressed in thousands of dollars and broken down by products from 1995-2012. From this source Armenia's exports in thousands of dollars to 16 countries: Germany, Belgium, Sweden, Italy, France, Netherlands, Bulgaria, Kazakhstan, Russian Federation, Belarus, Georgia, Iran, Ukraine, the USA, Canada and China with detailed product groups for 2012 was obtained. In the absence of official data for FOB values we set zero for missing values of FOB for particular product types in order to control for errors in the final calculations. Products in UNCTAD are classified according to Standard International Trade Classification (SITC) revision 3, which is converted by Harmonized Commodity Description and Coding System (HS), third edition 2002 taken from the website of United Nations Statistics Division. This is done in purpose to have correspondence with the tariff data for specific products taken from other sources which use HS 2002 for product classification. Tariff data for the USA, China, Canada, Ukraine, Georgia was obtained from the WTO website as it provides high quality tariff data at HS classification level. Tariffs of the EU (it has common external tariffs for all imported goods) were taken from European Commission Market Access Database by HS 2007 classification. Eurasian Custom Union's tariffs were found from the official website *Tsouz* which is now renamed *Eurasiancommission* at SITC rev.3 product classification. Finally, the tariffs of the neighboring Iran were obtained from the website of the Trade Promotion Organization of Iran again with the same classification.

The data on GDP (2012) and annual absolute value of exports of Armenia is collected from the sources of World Bank and Armstat, respectively.

3. Comparative analysis of three scenarios: CU, AA and SQ

3.1 Main Findings

Detailed description of three elaborated scenarios with tariff changes are crucial for the assessment of the gains or losses of Armenian exporters depending on countries decision to stay in SQ, or join CU or DCFTA.

In the first scenario where Armenia maintains its status quo, there is no tariff change; therefore there is no change also in gross revenue of the exporters. Average tariffs for all benchmarks such as machinery and equipment, manufactured tobacco, coffee and its substitutes stay unchanged for 16 countries. Armenian exporters when exporting to European Union member countries will continue to pay common external tariffs of the EU, which are the same for each country. The same way they will continue to pay CU's external common tariffs when exporting to the CU countries: Russia, Kazakhstan and Belarus and the tariffs of the remaining partner countries.

Thus, in the status quo scenario the fraction $\frac{1+t_1}{1+t_2}$ is equal 1, as there is no tariff change and $t_2 = t_1$.

The net revenue of the exporters is simply the multiplication of FOB_{value} with their revenue π (20% fixed):

$$NR_{SQ} = \frac{FOB_{value} * (1 + t_1) * (1 + \pi)}{1 + t_1} * \frac{1 + t_1}{1 + t_2} = \frac{FOB_{value} * (1 + t_1) * (1 + \pi)}{1 + t_1} * 1$$

$$= FOB_{value} * (1 + \pi)$$

Table 1 shows the FOB of exported goods to partner countries, gross and net revenues of the exporters after calculating imposed tariffs on products and adding 20% fixed revenue to that amount in status quo.

Table 1: FOB, gross and net revenues of the exporters in the Status Quo scenario

Countries	FOB	Gross Revenue	Net Revenue
Germany	154376	194361	185247
Belgium	126170	161670	151404
Sweden	8635	10362	10362
Italy	12462	16184	14954
France	5510	6982	6612
Netherlands	70445	86878	84534
Bulgaria	74880	92947	89856
Russia	282554	396779	339064
Kazakhstan	2061	2916	2473
Belarus	6599	9349	7918
Georgia	48989	66714	58786
Ukraine	17939	23231	21526
Iran	78112	97651	93734
Canada	7828	9890	9393
United States	12690	17023	15228
China	36493	45345	43791

In the second scenario Armenia decides to join Eurasian Customs Union of Russian Federation, Kazakhstan and Belarus. This CU applies common external tariff (CET) for third countries and eliminates tariff and non-tariff barriers among member countries. Thus, here tariffs are changed dramatically. All export tariffs with the members of the customs union are eliminated (are counted 0 in the analysis), and the tariffs with all other countries, including members of the EU, remained unchanged. In contrast with the status quo scenario where there was no tariff change, here the ratio of $1+t_1$ and $1+t_2$ varies depending on the percent of imposed tariffs on particular benchmark. For instance, if the tariff of the miscellaneous no-ferrous base metals for metallur currently is 15% when Armenia imports to Russia ($t_1=0,15$), after joining CU it will be 0 ($t_2=0$).

The ratio will be $\frac{1+t_1}{1+t_2} = 1,15$ higher than 1, which shows that the net revenue of the exporter of this product will rise. Therefore, if the sum of all net revenues of the exporters of exported products is compared with the sum of the revenues of status quo and AA, the losses or gains of the agreements will be apparent. Table 2 shows how net revenues were changed: the only change was in the CU members: Russia, Kazakhstan and Belarus where tariffs were eliminated.

Table 2: The sum of the net revenues of the exporters in SQ and when Armenia joins the CU

Countries	Net Revenue (Status Quo)	Net Revenue
Germany	185247	185247
Belgium	151404	151404
Sweden	10362	10362
Italy	14954	14954
France	6612	6612
Netherlands	84534	84534
Bulgaria	89856	89856
Russia	339064	396779
Kazakhstan	2473	2916
Belarus	7918	9349
Georgia	58786	58786
Ukraine	21526	21526
Iran	93734	93734
Canada	9393	9393
United States	15228	15228
China	43791	43791

Finally, in the third scenario Armenia decides to sign the Association Agreement with EU which is one of the points of Deep and Comprehensive Free Trade Agreement. As it was discussed above, in contrast with customs unions where members are obliged to impose CET on third country imports, in case of FTAs member countries are free in their external trade policies. This

FTA is not exclusion. If Armenia chose FTA with the European Union, then the tariffs of the imported goods in Armenia would stay unchanged, and at the same time the tariffs of Armenian exports to EU member countries would be eliminated.

Armenia will pay the CET tariffs when exporting to Russia, Kazakhstan and Belarus but 0 tariffs in Germany, Belgium, France and remained EU countries. Tariffs with other countries such as Georgia, Ukraine (if it is not in CU), USA, Canada, Iran and so on will not be changed. Hence, table 3 shows how in this scenario sum of net revenues of exporters will be changed if Armenia chose AA.

Table 3: The sum of the net revenues of the exporters in SQ and if Armenia signed AA

Countries	Net Revenue (Status Quo)	Net Revenue
Germany	185247	194357
Belgium	151404	161670
Sweden	10362	11456
Italy	14954	16184
France	6612	6982
Netherlands	84534	86878
Bulgaria	89856	92947
Russia	339064	339064
Kazakhstan	2473	2473
Belarus	7918	7918
Georgia	58786	58786
Ukraine	21526	21526
Iran	93734	93734
Canada	9393	9393
United States	15228	15228
China	43791	43791

Discussion of the Findings

This study is focused on the comparison of three above discussed scenarios for the assessment of Armenia's choice impact on the revenue of Armenian exporters. Current condition of Armenia, which is also considered as status quo is compared with two other possible choices of Armenia: CU and AA. Moreover, not only analyses are done for SQ vs. AA and SQ vs. CU but also CU is compared with AA.

The sum of net revenues of the exporters affected by the tariff changes of three scenarios are shown in Table 4. According to the table, it is apparent that countries which are not members of EU or CU will not see any changes in tariffs. Compared with the status quo, when Armenia joins CU the only change will be in tariffs in Russia, Kazakhstan and Belarus, where tariffs are eliminated. As EU have common external tariffs for all third non-member countries, it will not change its tariffs for Armenia, when it chooses CU. The same logic works for Eurasian Customs Union: if Armenia chose to continue implementing plans of Deep and Comprehensive Free Trade Agreement, Russia, Kazakhstan and Belarus will not raise their tariffs, as they have fixed external tariffs for non-member countries. Thus, by taking all these into account the calculated net wealth that Armenian exporters will gain when joining CU is 59.588.760. This amount involves net benefits coming from zero tariff trade with Kazakhstan, Russia and Belarus. Table 4 shows net benefits coming from each country separately when Armenia enters Customs Union.

It is apparent that Russia has the biggest share in this amount, and only Russia's share makes CU competitive with the EU's Association Agreement. In contrast with the Eurasian Customs Union where there are only 3 member countries, Association Agreement's impact can be higher as there are more than 7 countries trading with Armenia.

Table 3: Net revenues of exporters in 3 scenarios

Countries	Net Revenues (Status Quo)	Net Revenues (CU)	Net Revenues (AA)
Germany	185247	185247	194357
Belgium	151404	151404	161670
Sweden	10362	10362	11456
Italy	14954	14954	16184
France	6612	6612	6982
Netherlands	84534	84534	86878
Bulgaria	89856	89856	92947
Russia	339064	396779	339064
Kazakhstan	2473	2916	2473
Belarus	7918	9349	7918
Georgia	58786	58786	58786
Ukraine	21526	21526	21526
Iran	93734	93734	93734
Canada	9393	9393	9393
United States	15228	15228	15228
China	43791	43791	43791

Interestingly, the findings indicate that even in this case net wealth coming from Eurasian CU is more than AA. Table 5 points out how much net wealth Armenia could gain, if it signed AA with the EU. When compared table 4 and 5, we find out that in case when Armenia is in CU its exporters gain more than in AA or SQ.

Table 4: Net wealth in CU scenario (in thousands)

Countries	Net Revenues (Status Quo)	Net Revenues (CU)	Net Wealth
Russia	339064	396779	57714
Kazakhstan	2473	2916	443
Belarus	7918	9349	1431
SUM	349455	409044	59589

In the status quo exporters get \$ 349 million net revenues coming from CU members, while entering CU raises net revenues to \$ 409 million, where Armenian exporters will have net benefit of \$59 million. In the case of European Union, in status quo exporters get \$542 million net revenues, which means that, all in all Armenia’s trade with EU is more than with CU members. If Armenia signed AA, exporters would get \$570 million net revenues and compared with the status quo amount, net wealth coming from this agreement could be \$27 million, which is about 2 times less than the net wealth coming from CU (\$59 million).

Thus, we can summarize the gains coming from different scenarios based on the following findings:

- 1) $Gain_{SQ}^{CU} = NR^{CU} - NR^{SQ} = 409044 - 349455 = 59589$
- 2) $Gain_{SQ}^{AA} = NR^{AA} - NR^{SQ} = 570474 - 542969 = 27506$
- 3) $Gain_{CU}^{AA} = NR^{CU} - NR^{AA} = 59589 - 27506 = 32083$ (thousands \$)

Table 5: Net wealth in AA scenario (in thousands)

Countries	Net Revenues (Status Quo)	Net Revenues (AA)	Net Wealth
Germany	185247	194357	9109
Belgium	151404	161670	10266
Sweden	10362	11456	1094
Italy	14954	16184	1230
France	6612	6982	370
Netherlands	84534	86878	2344
Bulgaria	89856	92947	3091

SUM	542969	570474	27506
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This 32,083,000 absolute value shows how much is the difference between gains coming from AA and CU. As AA's gain is subtracted from CU's and the value is positive, this clearly shows that CU is more beneficial, and the difference shows how much it is beneficial.

In order to see what is the share of these gains in the GDP and exports of Armenia, ratios between these indicators are built. In these ratios it is noteworthy to mention that in 2012 GDP of Armenia was \$9.951 billion, from which 1.380 billion was the share of exports.

$$1) \frac{Gain_{SQ}^{CU}}{E} = \frac{59589000}{1380000000} = 0.04; \quad \frac{Gain_{SQ}^{CU}}{Y} = \frac{59589000}{9951000000} = 0.005,$$

$$2) \frac{Gain_{SQ}^{AA}}{E} = \frac{27506000}{1380000000} = 0.01; \quad \frac{Gain_{SQ}^{AA}}{Y} = \frac{27506000}{9951000000} = 0.002,$$

$$3) \frac{Gain_{CU}^{AA}}{E} = \frac{32083000}{1380000000} = 0.02; \quad \frac{Gain_{CU}^{AA}}{Y} = \frac{32083000}{9951000000} = 0.003.$$

These amounts apparently indicate that CU compared with SQ and AA is more beneficial when export is taken under consideration. Its share both in whole exports of Armenia and in GDP (0.04 and 0.005 respectively) is higher than Armenia could gain if it chose AA (0.01 and 0.002). If we compare both agreements with the Armenia's choice to preserve its status quo, it comes out, that both agreements are more beneficial than status quo. This is not surprising as in both agreements tariffs are eliminated, and zero tariff trade is always preferential than status quo with current tariffs. This is a case only when focus is on exports but not in imports, as in case of imports common external tariffs of CU can raise so dramatically that affect the gains coming from zero

tariffs of exports. When the gains of the Eurasian Customs Union and Association Agreements are compared, Armenian exporters benefit more when Armenia chooses to be in the CU scenario. All means for analyzing these scenarios indicate that gains coming from Eurasian Customs Union of Russia, Kazakhstan and Belarus are more than the benefits of AA. Similarly, the share of those benefits in the GDP and total exports of Armenia is more than the gains of AA, although these numbers are not significant for both AA and CU cases.

Conclusion

The aim of this work was analyzing comparatively the possible impacts of Eurasian Customs Union and DCFTA on Armenian exports. When three scenarios are taken into account one of the most immediately noticed impact of both FTAs is that they eliminate trade tariffs between member countries and make it more liberal among them. Based on this we found that these agreements are more beneficial for Armenian exports than being in the status quo and not joining any FTA. This is explained with the fact that 0 tariff trade will bring more gains to the Armenian exporters than in the scenario when they are obliged to pay some of their benefits as an import duty. As status quo is not a desirable solution for Armenia and at the same time two unions are incompatible with each other, the second question that arises is which one of these agreements is more beneficial. Based on our calculations of eliminated tariffs we found that CU will bring \$32 million more revenue to the exporters than DCFTA. In total, revenues coming from CU will be \$59, 6 million, and possible revenues that could come if Armenia signed AA would be \$27, 5 million. These are the numbers for the most extreme cases when variables such as transportation

costs, quantity of the exported goods, prices of the products, composition of the exports and non-tariff barriers are taken as fixed. These values show that exporters will gain more when Armenia is in the CU with Belarus, Russia and Kazakhstan. However, the next step of comparing these gains with the GDP or total exports of Armenia indicates that these benefits are making very small part of these components and are not significant at all. The share of the revenues coming from Russian-led Customs Union both in whole exports of Armenia and in GDP (0.04 and 0.005 respectively) is higher than Armenia could gain if it chose AA (0.01 and 0.002). However, even if its share is more than in the AA scenario, anyway numbers are not significant at all. This shows that Armenia is going to join a trade union where Armenian exporters will make only \$59.6 million more revenues or will increase Armenian GDP only by 0.005%. By taking this under consideration, it can be concluded that the claims that Armenia is going to benefit significantly from joining Eurasian Customs Union are not corresponding to the findings of this work, when export sector is taken into account. Thus, this study rejects three hypotheses examined in the work, stressing that nor CU, neither AA will bring significant revenues to Armenian exporters.

The research demonstrated that when compared with DCFTA Armenia have a little advantage in CU scenario, but at the same time there is an issue of common external tariffs and rise in import duties when Armenia becomes a member of CU. Hence, one of the main insights of the study was to contribute to the existing little literature by the finding that in export sector Armenia will not benefit in big proportions from joining Customs Union, and moreover, it will lose partially its trade sovereignty because of CET.

The work, however, has some limitations. First and the most important one is that import sector was not taken into account because of uncertainty of government redistribution policies.

Secondly export sector for only 16 the most exported product groups is analyzed, but there is a need also to take into account remaining product groups. And the last, but not the least is that factors such as non-tariff barriers of trade or sanitary standards are taken as fixed in all scenarios, while in reality depending on Armenia's choice these factors vary.

Based on those limitations there are several recommendations for further studies in this field. There is a need to examine possible impact of common external tariffs on Armenian imports, and to estimate how big will be the rise in average level of import tariffs. This is important for having whole picture of the possible effects of emerging CU on Armenian trade and to estimate whether there is any significant gain coming from this union. Secondly, it should be discussed what and how much Armenia will lost because of its not free access to the European markets. Finally there is a need to analyze Eurasian Customs Union not only as trade union, but also as political union.

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APPENDIX

Table 6: 16 product groups analyzed in the work

Products
Fish, fresh (live or dead), chilled or frozen
Crustaceans, mollusks and aquatic invertebrates
Vegetables, roots, tubers, prepared, preserved, n.e.s.
Fruits and nuts (excluding oil nuts), fresh or dried
Fruit, preserved, and fruit preparations (no juice)
Fruit and vegetable juices, unfermented, no spirit
Coffee and coffee substitutes
Non-alcoholic beverages, n.e.s.

Alcoholic beverages
Tobacco, manufactured
Other man-made fibres suitable for spinning
Other crude minerals
Ferrous waste, scrape; remelting ingots, iron, steel
Copper ores and concentrates; copper mattes, cemen
Ores and concentrates of base metals, n.e.s.
Non-ferrous base metal waste and scrap, n.e.s.
Ores & concentrates of precious metals; waste, scrap
Polyethers, epoxide resins; polycarbonat., polyesters
Miscellaneous chemical products, n.e.s.
Wood manufacture, n.e.s.
Lime, cement, fabrica. constr. mat. (excludingglass, clay)
Pearls, precious & semi-precious stones
Pig iron & spiegeleisen, sponge iron, powder & granu
Copper
Miscellaneous no-ferrous base metals for metallur
Metalworking machinery (excludingmachine-tools) & parts
Apparatus for electrical circuits; board, panels
Aircraft & associated equipment; spacecraft, etc.
Men's clothing of textile fabrics, not knitted
Women's clothing, of textile fabrics
Men's or boy's clothing, of textile, knitted, croche.
Women's clothing, of textile, knitted or crocheted
Articles of apparel, of textile fabrics, n.e.s.
Measuring, analysing & controlling apparatus, n.e.s.
Electric current
Glassware
Optical goods, n.e.s.