



Russia, Trade and the Rule of Law

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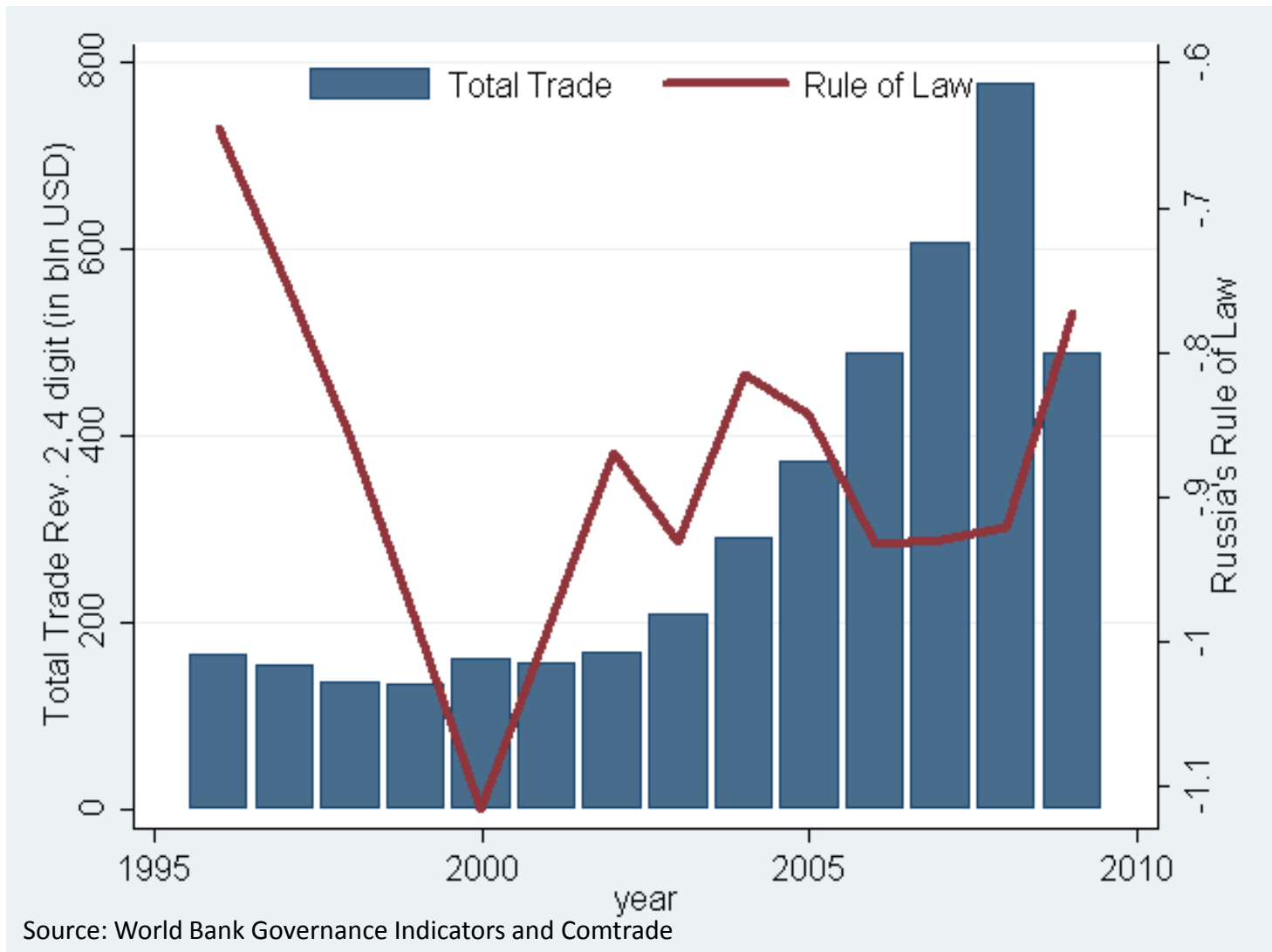
Why this seminar?

- EU-Russia relations still topical
 - Summit this week
 - Russia's WTO accession
- Dreyer and van der Marel (2014)
 - Economics of Transition
- Russia's wider economy
 - Energy, economic reform, etc.
- EU's policy responses / actions

Why this paper?

- IHT: “rule of law could harm Russia’s position as an economic partner in the world”
 - Is that really true?
 - And for what type of trade?
 - How does that affect Russia?
- Our findings are a “Yes, but...”
- Institutions do matter for the economy
 - Also for trade as a vehicle

Russia's Rule of Law



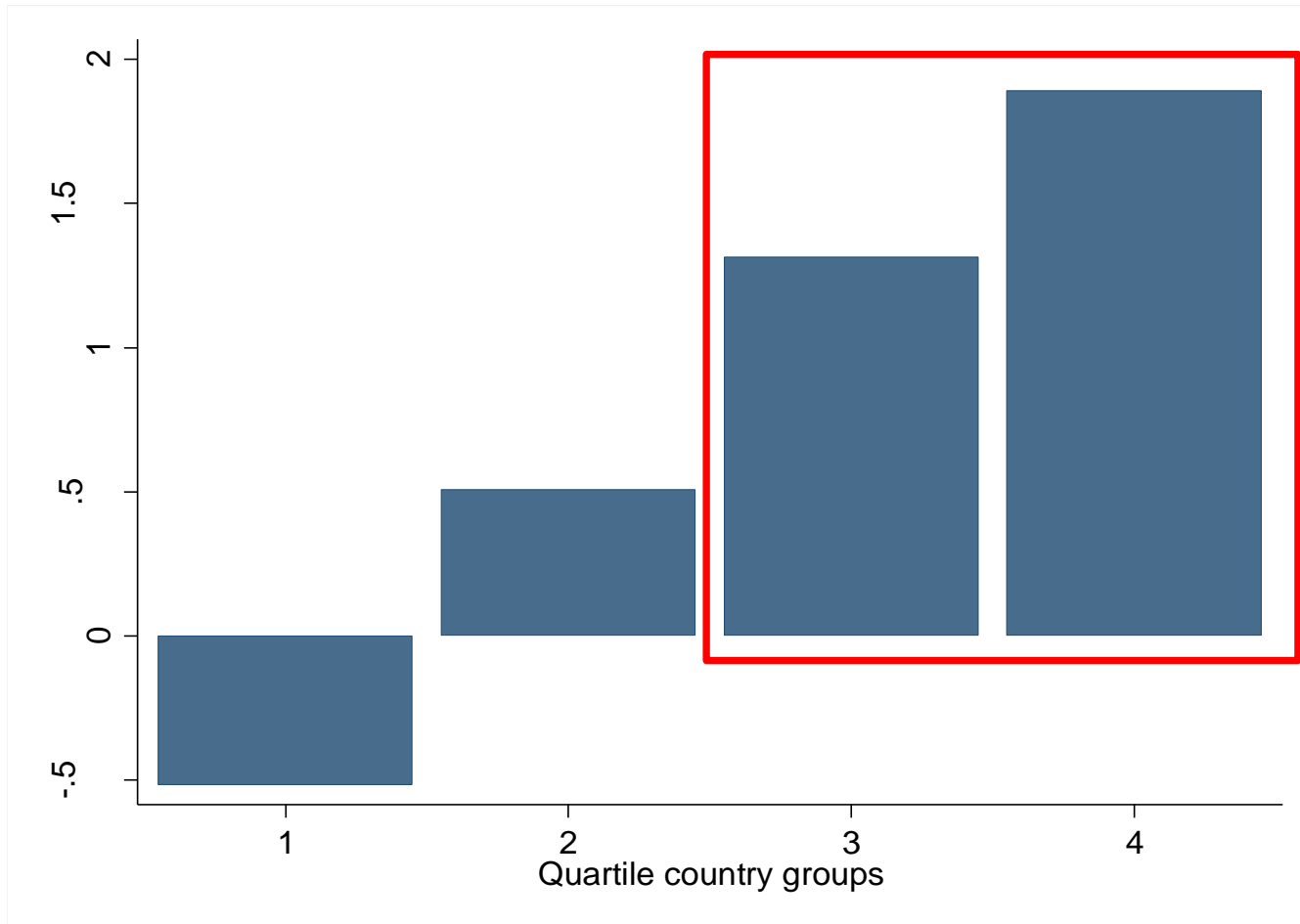
Russia's Rule of Law

- Does Russia's volatile rule of law have a negative effect on its trade and investment relations with partner countries, and if yes with who?
- Adverse effect is heterogeneous, i.e. differs across partner countries and sectors
- Expect to matter for those partner countries and sectors where rule of law is important.

Strategy and Data sources

- “Gravity” model as base, performed with PPML
 - Econometrical exercise, years 1996-2009
- Goods trade: Comtrade (UN)
- Services trade: Francois *et al.* (2009)
- Investment: Eurostat (not many partners)
- Rule of law: World Bank Governance

Partners' Rule of Law



Source: World Bank Governance Indicators

Partners' Rule of Law

- Quartile 4: USA, SWE, DNK, NLD, LUX, NZL, FRA, DEU, AUS, CAN, etc.
- Quartile 3: BEL, CZE, CYP, ISR, ITA, KOR, LTUE, MYS, POL, URY, etc.
- Represents 60-68 percent of Russia's (goods) trade
- These countries have best rule of law where trade could have an effect for Russia. Hence, where law is an important ingredient for economic activity. Why?

What type of sectors?

- For some sectors rule of law matters more .
 - Sectors in which Q4 and Q3 specialize
- So-called homogeneous vs. differentiated
 - Reference priced vs. consumer tailored
 - “Standard goods” vs. “sophisticated goods”
- Goods without gas included, technology goods
 - Crisis year 2009 in/excluded

Empirical Evidence

- Overall, a lower rule of Law since 2003 hurts Russia's exports and imports:
 - For mainly Q4 countries with highest rule of law
 - For those sectors which are “sophisticated”
 - Some evidence for Q3, but less strong
 - Hurts inward investment as well
 - But not so much services (data)

What is going on?

- Adverse effect of Russia's trade in advanced goods to developed country markets
 - Due to lowering rule of law
- Why? Advanced goods are more contract-dependent as opposed to standard goods
 - Many inputs cannot easily be identified in contract
 - “Relation-specific” trade and investment
 - Need strong enforcement mechanism

Policy Conclusions

- Wider context: institutions matter for economic growth and development
 - Russia's other governance institutions?
- Russia has so-called comparative advantage in technological goods? How to capitalize?
 - Technological goods rather sophisticated
- Overall economic and trade basket diversification important for competitiveness