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EXPERTS' MEETING ON TRADE AND INVESTMENT INTER-LINKAGES IN CAUCASUS AND CENTRAL ASIA

OECD Centre for Private Sector Development, Istanbul, 16 February 2004

SUMMARY OF PROCEEDINGS

The experts' meeting was jointly organised by the OECD Development Centre and the Directorate for Financial and Enterprise Affairs, with financial support from the Turkish Agency for International Cooperation and the Foreign Investment Advisory Service of the World Bank Group (see COM/DAFFE/DEV(2004)1). It gathered together some 30 participants, including four experts from each of the three countries under review (Azerbaijan, Kazakhstan and Uzbekistan), representing major research institutes and policy units involved in the area of trade and investment. Additional information is available at www.oecd.org/dev/ist.

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Economic structures and recent economic developments in Caucasus and Central Asia

1. All of the countries in the region having gained their independence at the end of 1991 subsequently experienced a difficult decade characterised by initial income declines of varying severity, and general increases in inequality and poverty.¹ Since the turn of the century the situation has been brighter: the fundamental transition from central planning has been completed and the countries have begun to experience economic growth. This growth does not, however, have a secure base. This is due to the presence of several common constraints such as heavy dependency on only a few export items, severe indebtedness and remoteness. Much still needs to be done to create well-functioning market economies that can deliver sustained growth with equity.

Major challenges to increase and diversify trade and investment

2. The discussion highlighted the importance of better investigating the complex linkages between trade, investment and governance in the region. In particular, participants from Azerbaijan, Kazakhstan and Uzbekistan agreed that:

- Natural resources will remain important and valuable export-earners in the near future. Resource-based activities are not necessarily a curse, in so far as governments are able to set up adequate institutional mechanisms to avoid or offset their negative effects (e.g. Dutch disease). Export proceeds can contribute to financing human capital formation, infrastructure and technological upgrading – which will in turn favour diversification.
- High transportation costs and insufficient trade facilitation are major impediments to trade and investment integration for these countries. Inadequate policies, administrative red-tape and lack of co-operation on transit and trade facilitation issues are, together with the physical barriers and lack of infrastructure, causing increased costs and delays. Countries in the region have signed numerous co-operation agreements; their implementation has however been incomplete.
- In policy-making, a lack of transparency and consultation with the private sector and civil society is proving to be a major obstacle to improving the policy stance, creating consensus and moving the reform agenda forward. Research organisations in these countries are under-resourced, lack recognition and their participation in policy design is extremely slight.
- WTO membership could bring about important gains, not only in terms of improved market access (which would be small, at least in the short run), but also (and probably more importantly)

1. For more details on recent economic developments in the region see R. Pomfret (2003), "Central Asia Since 1991: The Experience of the New Independent States", OECD Working Paper No. 212 (www.oecd.org/dev/wp).

in terms of the increased investment (foreign and domestic) that would follow as a result of the government signalling its commitment to transparent policies.

- The benefits from trade liberalisation are not automatic. Countries will only reap them if a sincere commitment is made to removing domestic distortions and improving public governance. Moreover, policy-makers in these countries must improve their understanding of the implications of the WTO agreements. Reinforcing capacities regarding trade negotiations is of crucial importance if countries are to minimise the risk of signing commitments that they are not able or ready to comply with or that are not coherent with their development strategy.

Instruments to address these challenges and achieve greater integration: WTO membership, regional co-operation, research and advocacy

3. Three general recommendations for the governments of these countries emerged:

- Complete domestic reforms and remove distortions in parallel with the opening up of the economy and WTO accession. Accession should be an integral part of a country's development strategy, a means to encourage domestic reforms, improve legal and regulatory systems and increase competitiveness.
- Foster regional co-operation, in particular in the area of trade facilitation, energy and water management, services and regulatory frameworks. Enhanced regional co-operation can contribute to establishing better institutions, policies, regulations and then foster development. Improved co-operation requires high political commitment and leadership as well as adequate resources and willingness at the lower, operational, level to implement agreements. There can also be great value from enhanced regional co-ordination (or even enhanced regional FDI policy integration) among governments competing to attract FDI.²
- Put in place more transparent and participatory policy-making processes. Donors and international organisations can help with capacity building initiatives for research organisations, such as involvement in joint projects, and can persuade governments of the importance of establishing formal consultation processes with all relevant stakeholders. On their side, these organisations could try to establish networks, both at home and across borders, in order to maximize their visibility and the impact of their research.

OECD activities relevant to the region

4. Participants agreed that OECD activities in the area of trade and investment are particularly relevant for the countries in Central Asia and Caucasus and can make an important contribution to sustaining their further integration into the global economy. In particular, participants agreed on the desirability of extending to these countries activities on trade capacity building (especially in view of their forthcoming accession to the WTO), on regional and multilateral strategies for developing trade in services, on bilateral and regional investment treaties and on investment promotion.

2. Such co-operation can help to increase both the effective size of the local market which investors are likely to be able to serve by investing in the region and the local market's perceived growth potential. Because co-operation helps to "tie the hands" of local politicians and policy-makers, it can also help to enhance the effective degree of policy and even political stability in countries throughout the region. Together, the more effective rule of law and improved FDI policy coordination among countries in the region should also greatly reduce the ability of local governments – and local "strong men" – to engage in corrupt and predatory activity vis-à-vis both local and foreign (potential) investors.

Follow up

5. There was a consensus on the desirability of launching one or more research projects on the following topics:

- The interplay between domestic policies and the impact of international trade liberalisation on the economies of the region. In particular, a strong interest emerged on best practices on WTO accession and the analysis of CIS countries' experience within the WTO.
- The potential for enhancing regional collaboration in areas such as regulatory practices, trade facilitation, energy and services.
- The factors that are hampering higher investment and the policy responses to overcome them.

6. These topics could be addressed within the framework of a joint project between the OECD and a network of local research centres, for instance in the context of the Development Centre's research project on policy interdependence and development outcomes (cf. DEV/GB(2004)1). Participants agreed on the usefulness of organising a follow-up meeting, where terms of reference for these studies could be drafted and responsibilities allocated. Azerbaijan offered to host such a meeting. As a first step, efforts will be made to enlarge the existing network of research institutes active in the region.