

THE TRADE WITH THE EUROPEAN UNION: PROGRESS DURING CRISIS?

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Summary

In the past few years the merchandise trade with the EU has had a positive trend, both in absolute and relative terms. Though 2009 has been characterized by the global financial and economic crises that inevitably affected the trade, our country's commercial relations with the EU had a relatively good evolution in such difficult times. But, beyond this positive finding, the analysis below shows that the reduction of the volume of commercial transactions with the European Union is in line with the trade recession at global and regional levels, and that various export categories having been affected differently. Finally, 2010 would probably be a post-crisis year – what trends will determine the development of bilateral trade?

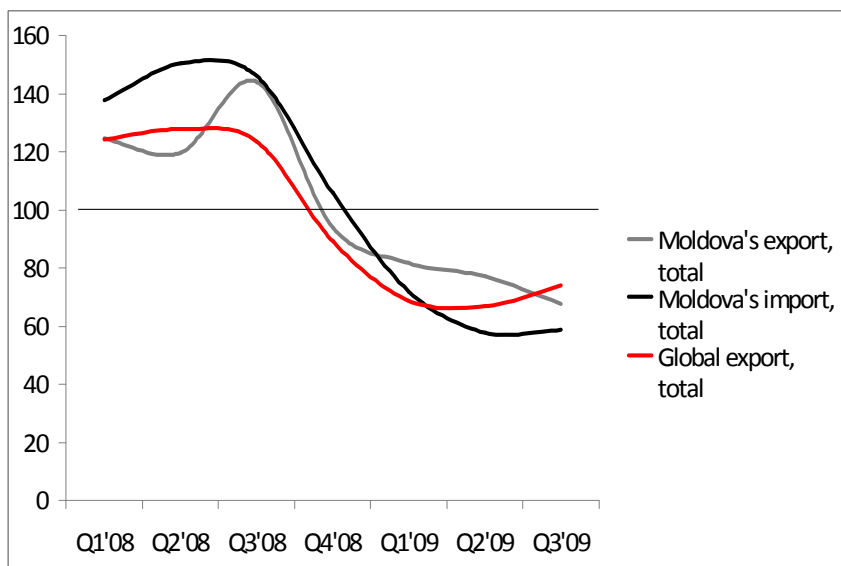
Foreign trade under crisis ...

As expected, the world economic crisis has seriously affected trade flows at global and regional level. For example, according to World Trade Organization data [1], the volume of world merchandise trade shrank 30% during the first three quarters of 2009, in annual terms. At the same time, EU exports decreased during the same period by approximately 30% and the CIS ones – by 45%. Simultaneously, the imports in the EU and CIS – Republic of Moldova's main trading partners, decreased dramatically – by 32% and 39% respectively. Certainly, given this situation, Moldovan foreign trade could not stay immune to external pressures. The main channels that fueled the impact were:

- The decrease of internal demand in countries that are Moldova's main trade partners (expressed in a decline of their total imports) led to a weaker demand for Moldovan exports; as secondary effect, exporting companies reduce their investments activities, which in its turn affects employment and the process of buying new equipment, thus influencing Moldovan demand for imports;
- The local demand compression in Moldova, as a result of a drop in remittances from Moldovan migrant workers, hit by the decline in demand for their services in the respective host countries affected by crisis as well;
- The crisis has negatively influenced the crediting process, thus limiting the access to financial means, necessary for consumers and trade intermediaries.

Therefore, during the same period, Moldovan merchandise exports decreased by 25.1% and imports - by 37.8% [2] (Figure 1).

Figure 1. Quarterly development of Moldovan and global exports and imports, in annual terms, Q3'08-Q3'09.

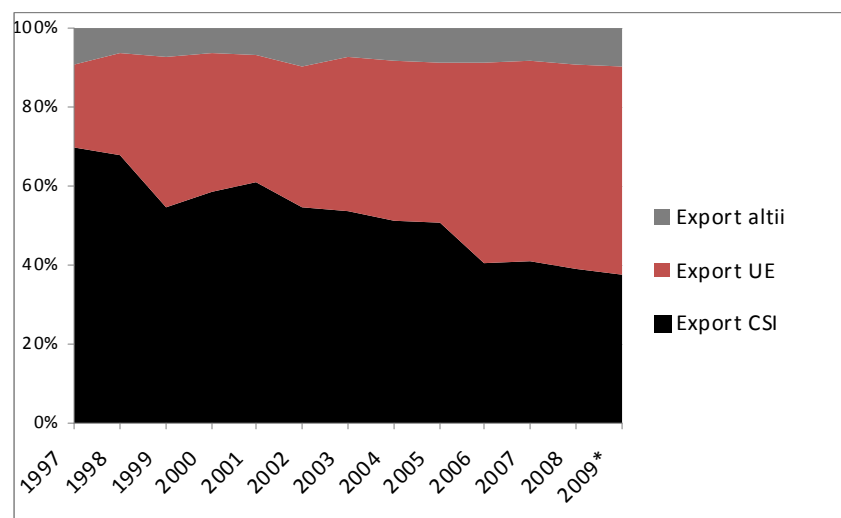


Source: NBS, WTO.

Exports remain Europe-centered...

Though the world economic crisis has seriously affected Moldovan exports, it has not altered their trend during the last decade: the geographical reorientation to the common European market. As one can see in the figure below, this process continued during the first ten months of 2009. In this period, the share of exports to the European market increased by 1,1%, from 51,6% to 52,7%, as compared to the same period last year. This increase was due to exports to the CIS, quotas for other countries remaining unchanged.

Figure 2. Geographical trend of Moldovan exports' share, 1997-2009.



(*the months of January-October)

Source: NBS, authors' calculation.

This trend was set by a series of basic and conjuncture factors. The basic factors refer to: trade liberalization at the beginning of the transition period; the economic recovery after the transformational recession and an obvious exports' „gravity” towards neighboring European markets with great purchasing power. Another basic factor was characterized by a successive liberalization of the trade regime between the EU

and the Republic of Moldova: from GSP (1999) through GSP+(2006) and up to Autonomous Trade Preferences granted by the EU in March 2008 [4].

Conjuncture factors at various stages have been expressed in trade shocks, such as the Russian crisis from 1998 or the „wine embargo” set up by Russian authorities in March 2006. Both shocks have had a strong impact on Moldovan exports to the Russian market and „contributed” to their reorientation towards more predictable European markets. In this context, the global economic crisis can be attributed to this series of factors (although, it is to be seen how sustainable its effects would be). The fact that the trade partners in the CIS have been more severely hit by the global crisis determined a more pronounced compression of exports to these countries.

The mostly affected trade markets in the EU [5] are the Polish and Romanian ones, which registered a drop in exports of 45% and 30.9% respectively during the first ten months of 2009. Compressions, as drastic as the first ones, were also registered on some CIS markets - the Ukrainian one (-47.8%) [6] and Kazakhstan (-43%). While the effects of the global economic crisis on Ukrainian and Romanian economies were absolutely „spectacular”, with GDP reductions of about 14% and 8% in 2009, Kazakhstan and even to a greater extent Poland succeeded to end this crisis year relatively „unharmed” (Poland will even register positive economic growth in 2009).

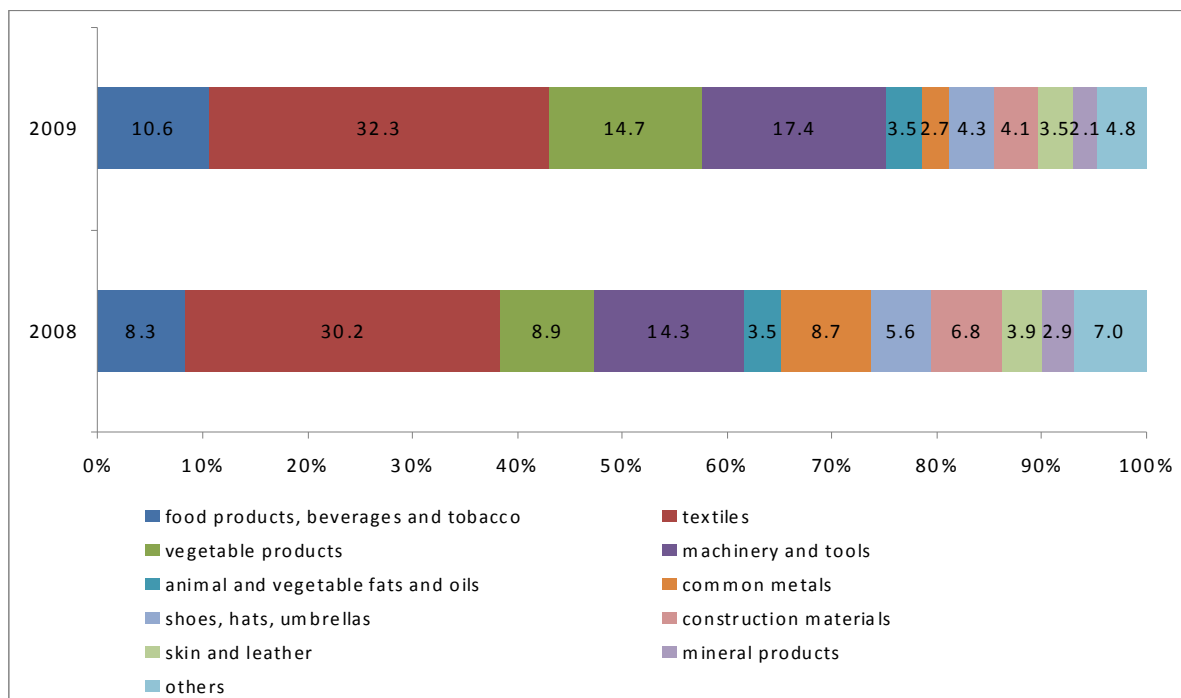
Simultaneously, a look to the evolution of total imports in the above-mentioned countries point out to developments, generally similar to Moldovan imports. For example, in January-October 2009 total imports to Ukraine and Romania decreased 52% and 41%, respectively [7]. These reductions exceed the ones of Moldovan exports to these countries. What concerns trade relations with Romania, these indirectly confirm the assumption that the decrease in volume of Moldovan exports to Romania was due to a worsening of political relations between the two states and the introduction of the visa regime for Romanian citizens.

Overall, exports to Romania (as well as to other states in Central and Eastern Europe) have been more severely affected by the global economic crisis that negatively influenced local demand, but to different extent for various groups of goods. Thus, such exports as textiles, shoes, construction materials and metals with significant shares in Moldovan exports to Romania have dramatically decreased during the crisis, while exports of machinery and equipment, oil seeds or sugar considerably increased. Apparently, this is the reason why Romania was outrun by the Russian Federation in the rating of Moldova’s export destination countries. At the same time, the share of agricultural food products in overall exports was bigger for exports to Russia and these better resisted the crisis, thus advancing again Russia among the top export destinations for Moldovan products[8].

Another important factor with adverse effects on the trade relations with Central and Eastern European, as well as CIS countries was the evolution of the exchange rate. While national currencies in Russia, Ukraine and Romania started devaluing (by over 30% in the first half of the year after the crisis start), the Moldovan leu „enjoyed” an unprecedented stability in the region. This has also undermined the competitiveness of Moldovan exports, as compared to the countries that devalued their national currencies.

The crisis had a significant impact on the structure of Moldovan exports that consequently led to certain changes in their configuration on the European market. The analysis reveals that the mostly affected categories referred to ordinary metals (-77.2%) and construction materials (-59%) – a fact that is easy to understand, given the collapse of the constructions sector in many Central and Eastern European countries, including Romania. On the other hand, the agro food products were the most resistant to crisis, registering less significant drops – food products and beverages (-13.1%), or even considerable increase, like in the case of vegetal products (+25%). The prospects for agro food products are still optimistic, given maintenance, among others, of relatively high prices for food products at global level and the removal of a series of institutional barriers in the Republic of Moldova. Simultaneously, the development of „losing” categories will greatly depend on the economic recovery in the region. However, a spectacular revival of such exports is hardly possible.

Figure 3. Dynamics of the share of Moldovan exports (%) on the EU market, January-October, 2008-09. .

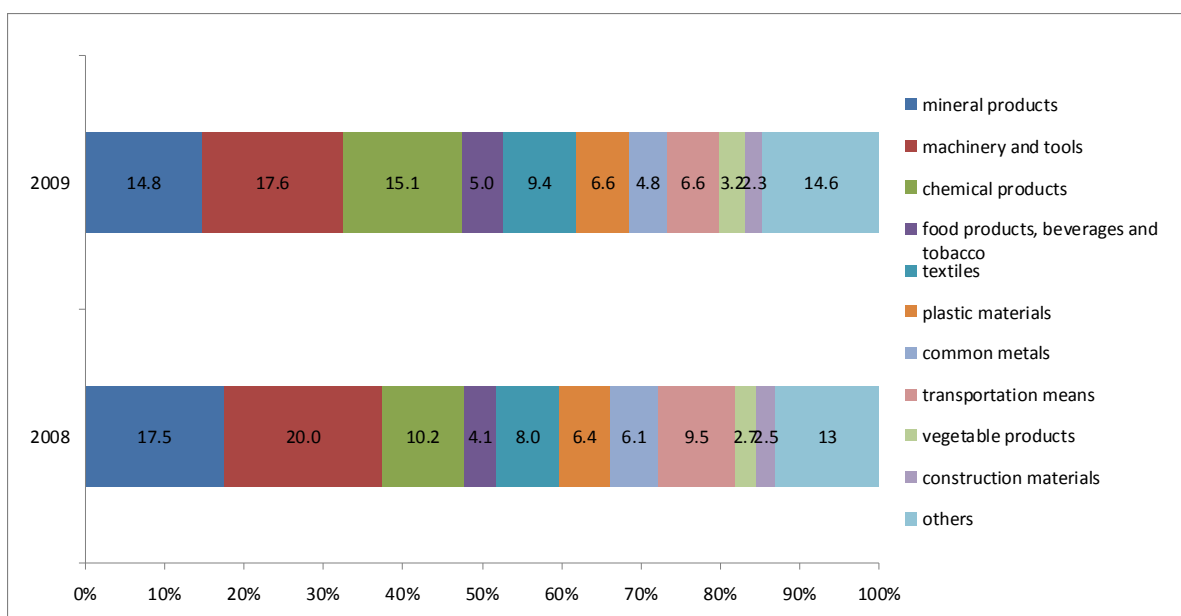


Source: NBS, author's calculation.

Imports: an even decrease...

Unlike exports, the imports' decrease has been quite even from a geographical point of view: the share of EU imports decreased by 0.2% and those from CIS – by 0.1%. Generally, exports from EU dropped by 22.5% during the first ten months of 2009, reflecting both a decrease in demand in Moldova, and a reduction of the unit value of imported products, such as oil products.

Figure 4. Development of the share (%) of various imports from the EU to the Moldovan market, January-October, 2008-09.



Source: NBS, author's calculation.

This was one of the main factors leading to the compression of Romanian imports to Moldova [9]. Among the European countries with relatively significant shares in total imports, the most considerable decrease has been noted for imports from Romania (-53%), Poland (-34.4%) and Germany (-35.2%).

Simultaneously, the structure of imports has also suffered some changes in the first ten months of 2009. It is worth noting, that besides „livestock and animal products”, all import categories from EU decreased more or less. This is a result of the local demand compression, caused first, by a significant decrease in the volume of foreign remittances (one example is the considerable decrease by 55% in transportation means' imports), as well as the shift in price strategies on world markets, like in the case of mineral products.

A view into 2010...

In 2010, the development of trade relations with the European Union will be shaped by a number of factors:

- *European countries' economic recovery.* Most probably, the economic recovery (if the second wave of the crisis is avoided) will be a slow one, with reduced investments and a feeble creation of new jobs. Another important aspect relates to the fact, how quick would be Central and Eastern European, as well as Southern economies in overcoming the stringent structural problems, amplified by the current crisis. In this case, Moldovan companies would have to be ready for a very slow demand recovery in the EU and try to reclaim their positions through competitive advantages.
- *Moldovan Government's capacity to eradicate institutional barriers for exports.* Aside from problems pertaining to competitiveness, Moldovan exports face a number of institutional barriers, either specific to the branch or related to customs issues. Only when the Government succeeds to remove a major part of these barriers (as in the wine sector), Moldovan exports would be given a relatively important „boost”, at least short and medium-term;
- *The capacity of Moldovan competent ministries and private entities to ensure the conformity with European standards, especially with sanitary ones.* For quite a long period of time Moldovan exports of animal origin products are being banned. These cannot benefit of the PCA stipulations on duty and quota free access on the European market. A success in this area, that would have to refer, among others, to the reorganization of the competent ministry and agencies, would help Moldovan local producers to diversify their markets and increase profits;



- *The internal demand recovery in Moldova.* The prospects for the recovery of internal demand in 2010 are tightly related to the recovery of the remittances' volume. But, this is also dependant on the re-

One should also note another important development with impact on trade relations between the European Union and Republic of Moldova is the process of negotiating the Deep and Comprehensive Free Trade Agreement. The Moldovan Government's preparedness for the round of negotiations will determine the efficiency for promoting the economic interests of Moldovan companies and consumers. However, it is absolutely crucial for narrow interest groups of some local producers not to prevail over larger (less promoted) groups of consumers.

Sources:

- [1] http://www.wto.org/english/res_e/statistics_e/quarterly_world_exp_e.htm, last check – December 23, 2009.
- [2] Hereafter, the national statistical data is taken from the NBS.
- [3] According to the basic gravity model, the amount of bilateral trade between two countries is to a large extent related to their economic size (GDP) and the distance between the two countries..
- [4] Quotas foreseen within these preferences are used completely before the year-end for a number of products, such as: wine, sugar, corn, and wheat. A more comprehensive liberalization of the trade regime with EU would allow for an increase of such exports. At the same time, Republic of Moldova cannot use these preferences for products of animal origin, because of the country's incapacity to meet the sanitary standards of the EU regulatory framework. In 2010, the export of honey will be unblocked. It was banned in 2008, because of forbidden substances found by European experts in Moldovan honey. For more information, see MEGA I and II, Expert-Grup, 2009.
- [5] With a relatively significant share (above 3%) in total exports.
- [6] Hereafter, the estimate on GDP compression is taken from the *World Economic Outlook, IMF, October 2009* .
- [7] WTO, idem.
- [8] For more information, see *MEGA II*, 2009 and *Romania – Republic of Moldova: The analysis of bilateral economic relations*, 2009, both by Expert-Grup.
- [9] Also see *Romania – Republic of Moldova: The analysis of bilateral economic relations*, 2009, by Expert-Grup.



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ADEPT's mission is to promote the democratic values and support citizen active participation in public affairs.

Strategic Objectives

- Contribute to the efficient implementation of the governmental strategies aimed at the socio-economic development and democratization of Moldova;
- Promote and consolidate the democratic institutions and procedures;
- Encourage and facilitate citizen participation in the decision-making and governance processes.