

# **Results of the analysis regarding the perspective of closer trade and investment relations between the Russian Federation and the EFTA States**

*The digest of the report of the Russia-EFTA joint study group<sup>1</sup>*

The Joint Russia-EFTA Study Group (JSG) undertook a comprehensive study of existing bilateral economic linkages between Russia and the EFTA States, covering trade in goods and services, investment flows and other areas of economic co-operation, with a view to examine ways and means to foster closer trade and economic ties between the two sides. The parties exchanged statistical data on trade and investments, information on bilateral agreements as well as on their approaches to the establishment of the preferential relations with third countries.

## **I. Regional and bilateral arrangements**

### **Russia**

Russia's current preferential trading arrangements are largely focused towards the CIS countries. Russia currently has bilateral FTAs on trade with all CIS countries. Preferential trade represented 23% of Russia's total imports and 15% of total exports in 2007. Free trade agreements with CIS Member States covered respectively 85 and 99% of Russia's actual imports from, and exports to, CIS countries in 2007, which were duty free.

In 1999 the Agreement on the Creation of a Unified State was concluded between the Russian Federation and the Republic of Belarus. Currently a free trade agreement is in force and both countries are in the process of creating a customs union.

Furthermore, Russia is a party to several regional arrangements in the post-Soviet space. One of these – Eurasian Economic Community (EAEC)<sup>2</sup> – was established in 2000 by the Agreement on the Establishment of the Eurasian Economic Community, which entered into force in 2001. The objective of the liberalisation process within the EAEC framework is to establish a customs union and a single economic space. This objective will be pursued in stages, taking into account the Parties' preparedness for different levels of integration.

### **EFTA**

The European Free Trade Association was established in 1960 on the basis of the Stockholm Convention, creating one of the first free trade zones (goods). A revised Convention (Vaduz Convention) entered into force in June 2002 with strengthened provisions for relations between the four EFTA States in the areas of trade in services, investment, public procurement, intellectual property, movement of persons, recognition of professional qualifications, and providing for an enhanced common platform for relations between the EFTA Member States and third countries.

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<sup>1</sup> The Joint Study Group was established by Ministers of the EFTA States and the Russian Federation on 2 December 2007 and its report was issued on 17 November 2008.

<sup>2</sup> EAEC comprises Belarus, Kazakhstan, Kyrgyz Republic, Russia and Tajikistan.

The economic relations of the EFTA States with the European Union are governed by the Agreement on the European Economic Area (EEA) for Iceland, Liechtenstein and Norway, and by a Free Trade Agreement (1972) and additional bilateral agreements for Switzerland.

By the time the JSG had finalised its report, EFTA had 15 fully operational FTAs, comprising 19 countries (excluding the European Union). These include Croatia and Macedonia in Europe, and Egypt, Israel, Jordan, Lebanon, Morocco, the Palestinian Authority, Tunisia and Turkey in the Southern and Eastern Mediterranean region. Partners in other parts of the world comprise Chile, Mexico, the Republic of Korea, Singapore, and the South African Customs Union (composed of South Africa, Botswana, Lesotho, Namibia, and Swaziland). EFTA signed a FTA with Canada in January 2008.

Negotiations with the 6 countries of the Gulf Co-operation Council (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates) were finalised in April 2008. EFTA concluded negotiations with Colombia in June 2008<sup>3</sup>. When the JSG finalised its report, EFTA was in negotiations with four countries: Algeria, India, Peru, and Thailand. EFTA has concluded Joint Declarations on Co-operation with Albania, Mongolia, Serbia, Ukraine and MERCOSUR (Argentina, Brazil, Paraguay and Uruguay). A Joint Feasibility Study had been concluded with Indonesia.

On a bilateral basis Japan and Switzerland confirmed on 29 September 2008 that they have reached an agreement in principle on an Agreement on Free Trade and Economic Partnership<sup>4</sup>. Bilateral FTA negotiations were ongoing between Iceland and China. Norway and China had finalised a Joint Feasibility Study and had held a first round of FTA negotiations in September 2008.

## **II. Overview of the bilateral trade and investment co-operation between the Russian Federation and the EFTA States**

### **1. Trade in goods**

Bilateral trade between Russia and the EFTA States in 2007 stood at about USD 17 billion (according to Russia as the reporting country) or 6.8 billion (as reported by the EFTA States), accounting respectively for 3.2% of Russia's overall trade with the world and for 1.2% of EFTA's overall trade with the world. Among the EFTA States Switzerland is the largest trading partner of the Russian Federation.

There are clear differences in the statistics reported by the EFTA States and Russia. The trend in trade flows between the two partners is, however, similar across both sets of statistics: total trade (value terms) between EFTA and Russia has increased steadily over the last five years.

Russia recorded in 2007 imports from the EFTA States at a value of USD 2.8 billion, an increase of 12% over 2006, and exported goods to the EFTA States worth USD 14.6 billion, an increase of 14% over 2006. Excluding all Russia's FTAs currently in force, the EFTA States were Russia's 8<sup>th</sup> largest import source in 2007, after the EU, China, Japan, USA, South Korea,

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<sup>3</sup> Signed in November 2008.

<sup>4</sup> The Partnership Agreement between Switzerland and Japan was signed in February 2009. Switzerland has also undertaken to do a Joint Feasibility Study with China.

Turkey and Brazil, and Russia's 4<sup>th</sup> most important export destination, following the EU, Turkey and China.

The EFTA States recorded imports from Russia amounting to USD 3.3 billion in 2007, an increase of 7% over 2006, and exports to Russia amounting to USD 3.5 billion, an increase of 28% from 2006. Russia was EFTA's 6<sup>th</sup> largest import source in 2007, after the EU27, US, China, Japan and Canada, and EFTA's 7<sup>th</sup> most important export destination, following the EU27, US, Japan, Canada, China and Hong Kong (China).

The tables below provide trade statistics according to Russia's and EFTA's sources.

**Table 1: Russia-EFTA Trade Overview 2003-2007 (USD billions)**

Year	Russian Federation as the Reporting Country			EFTA States as the Reporting Country		
	Imports from EFTA	Exports to EFTA	Total trade	Imports from Russia	Exports to Russia	Total trade
2003	0.9	3.9	4.8	1.8	1.2	3.0
2004	1.2	5.3	6.5	2.0	1.5	3.5
2005	1.7	8.9	10.6	2.1	2.1	4.2
2006	2.5	12.8	15.3	3.1	2.7	5.8
2007	2.8	14.6	17.4	3.3	3.5	6.8

Source: RF Federal Customs Service's statistic data;, GTIS, Global Trade Atlas

## 1.1 Industrial goods

According to Russian statistics, taking the EFTA countries together, the **main commodities traded** (imports and exports) between Russia and the EFTA States in 2007 included mineral fuel and oil, fish and seafood, nickel, pharmaceuticals, machinery (reactors, boilers), and precious stones. Russia's main export commodities to the EFTA States were mineral fuel and oil, nickel, precious stones, copper, inorganic chemicals and rare earth metals, aluminium. The key import commodities from the EFTA States were fish and seafood, pharmaceuticals, machinery, electrical machinery, optical, medical instruments and clocks and watches.

According to EFTA's data taking the EFTA countries together, the main commodities traded (imports and exports) between EFTA and Russia in 2007 included aluminium, fish and seafood, precious stones, pharmaceuticals, and machinery (reactors, boilers). EFTA's main export commodities to Russia were fish and seafood, pharmaceutical products, machinery, electrical machinery, clocks and watches, precious stones, and optical, medical instruments. The key import commodities from Russia were aluminium, precious stones, inorganic chemicals and rare earth metals, mineral fuel and oil, and iron and steel.

## 1.2 Agricultural goods

With respect to trade in agricultural goods, bilateral trade between Russia and EFTA States grew robustly between 2005 and 2007.

The value of total trade in agricultural goods amounted to USD 143 million in 2007, an increase of 29% over trade recorded in 2006 (Russia as the reporting country). Russia exported agricultural products to the EFTA States worth USD 18 million in 2007, up 95% from 2006 and imported agricultural products from the EFTA States worth USD 125 million, a rise of 24% from 2006.

EFTA reported that total trade in agricultural goods with Russia amounted to USD 125 million in 2007, a 47% increase from 2006. EFTA exported agricultural goods valued at USD 108 million to Russia and imported agricultural products from Russia valued at USD 16 million.

As reported by the EFTA States, *Switzerland's* largest agricultural export item to Russia in 2007 (55% of overall bilateral agricultural exports) was miscellaneous food items (mainly coffee based products), followed by baking related items (23%) and cocoa (7%). *Norway's* leading agricultural exports were cheese and other dairy products (20% of exports to Russia), followed by other products of animal origin (19%) and meat (17%). *Iceland's* main agricultural exports to Russia in 2007 consisted of dairy products (42%), followed by sugar confectionery (26%).

Russia's most important agricultural exports to the EFTA States in 2007 were as follows: Tobacco represented the largest agricultural export item to Switzerland (accounting for 59%) – followed by fats and oils (18%), and beverages (10%). Norway's leading agricultural import item from Russia was fats and oils (60%), followed by food waste (21%), and milling, malt, and starch products (9%). Iceland's main agricultural imports from Russia in 2006 consisted of tobacco (85%) and beverages (11%).

According to Russia's statistics the leading agricultural exports to the EFTA States in 2007 were tobacco, constituting 53% of its exports to Switzerland. Other products included raw fur skins (28%), wheat and meslin (8%) and undenatured ethyl alcohol (5%). The most important agricultural exports to Norway in 2007 were rye (59%), wheat and meslin (17%), wheat gluten (15%) and oilcakes of vegetable fats and oils (9%). The main agricultural exports to Iceland in 2007 were cigars and cigarettes (91%) and undenatured ethyl alcohol (9%).

As regards agricultural imports from the EFTA States, according to Russia's statistics, the leading agricultural import items from Switzerland in 2007 were as follows: tea and coffee based products constituted 40% of Russia's overall agricultural import from Switzerland, followed by malt extract (23%) and chocolate and other food preparations containing cocoa (8%). The most important import items from Norway in 2007 were miscellaneous food products (57%), soya oilcakes (8%) and cheeses (6%). Iceland's main agricultural exports to Russia in 2007 were sugar confectionery (12%) followed by meat (7%) and milk and products thereof (6%).

## **2. Trade in Services**

Trade in services between Russia and the EFTA States reached USD 2.86 billion in 2006, according to figures provided by the Central Bank of Russia. These statistics cover trade in services in modes 1 and 2 only (cross border trade and consumption abroad). Overall, the most important sectors were transport and business services, representing over 50% of total bilateral services trade.

Between Russia and Norway, the travel sector (aggregate expenses of physical persons for goods and services for private consumption in the territory of a foreign country during trips

from permanent location) accounts for about one third of Russian exports to Norway, and for 63 % of Norwegian exports to Russia. Other important sectors in bilateral services trade are energy related services and “Other business services” (including operational leasing services, business, professional and technical services), which make up for about 30% of Russian exports to Norway and 23% of Russia’s imports from Norway.

With regard to Iceland, the main sectors in bilateral services trade in 2006 were “Other business services” (47% of Russian exports and 61% of imports), as well as travel (35% of exports, 30% of imports).

Switzerland ranks among the ten major trading partners of the Russian Federation in services. In 2006, exports of services from Russia to Switzerland amounted to USD 1.3 billion (about 5% of Russia’s total services exports), while imports from Switzerland amounted to USD 1.1 billion. Transport services accounted for 54% of Russian services exports to Switzerland, but only 13% of imports. The main sectors for imports from Switzerland were travel and “Royalties and license fees<sup>5</sup>”. These sectors cover 56% of total Swiss services exports to Russia.

Regarding mode 4 (presence of natural persons), the number of EFTA States’ nationals having obtained work permits in Russia totalled 412 in 2006 (234 Swiss, 166 Norwegian and 12 Icelanders), increasing to 575 in 2007. Most were engaged in activities connected with wholesale and retail trade services.

Among the existing bilateral arrangements, the Russia-Switzerland Agreement of 12 May 1994, the Russia-Norway Agreement of 26 March 1996 and the Russia-Iceland Agreement of 2 July 1982 do not affect trade in services in a significant manner.

As to sectoral agreements between Russia and individual EFTA States, Russia and Norway have the following bilateral agreements: on air communication (1956); on maritime transport (1975); on cooperation in the area of mail service (2002); on road transport (2005); and on simplification of issuing visas (2007). Russia and Switzerland have the following bilateral agreements: on road transport (1989); and on regular air communication (1993). Russia and Iceland have a bilateral agreement on air communication (1998).

### **3. Investment**

The EFTA States are substantial investors abroad and receive significant amounts of inward investment.

Bilateral investment between Russia and the EFTA States is growing, albeit from a relatively low base. According to calculations by the Russian Statistical Service (ROSSTAT), the aggregate share of investments by EFTA companies amounted to 3.4% of total accumulated foreign investment in Russia. Foreign direct investment (FDI) flows from Switzerland to Russia, as reported by the Swiss National Bank, increased from USD 95 million in 2002 to USD 1’062 million in 2006; FDI stocks in Russia reached USD 4.1 billion in 2006, representing 0.8% of total Swiss FDI abroad. Switzerland, as per Russian statistics, is Russia’s largest investment partner among the EFTA States, and 9<sup>th</sup> largest in the Russian economy as a whole. Switzerland is also a recipient of Russian outward FDI, which doubled between 2005 and 2007. Norwegian FDI into Russia has seen continued growth in recent years, reaching, according to Statistics Norway, approximately USD 1.4 billion in 2006 from USD 1.2 billion in 2005. Russian FDI into

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<sup>5</sup> “Royalties and license fees” includes authorized use of land and natural resources, license fees, patents, “know-how”, trademark, brands etc.

Norway is low and has been falling in recent years. Icelandic FDI into Russia is relatively small, as is Russian FDI into Iceland.

Key sectors of Swiss FDI in Russia today are the metallurgical and chemical industries. Substantial Swiss capital is also invested in the food industry, in wood-processing and in agriculture. On the other hand, Russian capital in Switzerland is mainly concentrated in real estate and the leasing industry, with portfolio investment largely prevailing over direct investment.

The major part of Norwegian FDI in the Russian economy is found in the manufacturing industry (about 35%), mining, wholesale and retail trade. Russian capital in Norway is primarily invested in manufacturing and mining. Icelandic investment into Russia mainly takes the form of portfolio investment and is concentrated in the real estate sector.

Bilateral agreements on the promotion and protection of investments (BITs) exist between Russia and Norway and Switzerland, respectively. Negotiations on a BIT between Russia and Iceland are currently under way. All of these agreements primarily contain traditional disciplines on the treatment and protection of legally admitted investments (“post-establishment phase”). Additionally, Norway and Switzerland have an agreement on the avoidance of double taxation with Russia.

The Ministry of Economic Development of the Russian Federation is one of the main authorities responsible for formulating and implementing the investment policy of the Russian Federation. The current policy in this area is aimed at creating conditions to promote the expansion of domestic and foreign investments, and also at formatting transparent and stable rules in the conduct of economic activities.

### **III. Conclusions**

Trade statistics show that there are complementarities in the sector-specific strengths of the EFTA and Russian economies respectively, as evidenced by the nature of current trading patterns, which may be further developed.

There is potential for growth in trade and investment flows between the EFTA States and Russia in those sectors in which each partner has a particular strength.

The JSG found significant potential for Russia and the EFTA States to advance their economic relationship further, and came to a positive conclusion with respect to the feasibility of establishing a broad-based free trade agreement.