



Russia in World Trade

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Highlights

- Transition has increased Russia's openness and trade, but Russia is still a medium-sized trader and not a giant in the field. However, Russia is a very large commodity exporter.
- Russia's foreign trade grew exponentially from 1991 to 2012, and then slowed down. Fuel exports with rising commodity prices were a strong driver and led to fluctuations over time.
- During the first stage of transition, Russia turned to Western Europe, and later China entered the field, both at the expense of trade with the former Soviet Union (FSU). Russia has benefited from China's growth and could likely benefit from further trade integration with Western Europe as well as China.
- Russia's WTO accession took 19 years and led to liberalisation for trade in goods and important institutional reforms. But Russia's regime for services trade and foreign direct investment (FDI) is more restrictive.

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- The Eurasian Economic Union (EAEU) is an important achievement, but trade with the FSU area had slow growth, and Western Europe and China are Russia's most important trade partners.
- In the early 2020s, geopolitical tensions and security issues, including the Russia-Ukraine conflict, are limiting Russia's trade policy development. The green transition may also be a future key issue for Russian trade, with carbon border taxes and the phasing out of fossil fuels on the global agenda.

12.1 INTRODUCTION

During the Soviet period, foreign trade was heavily regulated and limited. The rouble was not convertible, so trade was not possible without special permission to use foreign currency. In 1989, the foreign trade of the Soviet Union amounted to 15% of the gross national product (GNP), and more than half of its foreign trade in goods was with members of COMECON or Council for Mutual Economic Assistance (CMEA).^{1,2} At this time, trade within the FSU area was domestic and not counted as international trade.

After the fall of the Iron Curtain in 1989, COMECON and the Soviet Union were dissolved in 1991. The collapse of the central planning system led to the external opening and increased trade with the whole world, and particularly Western Europe. A major event was Russia's membership in the World Trade Organization (WTO) from 2012, following a 19-year period of preparation and arduous negotiations starting from 1993.

At the same time, Russia pursued the aim of continued economic integration in the FSU area, with several steps from the Commonwealth of Independent States (CIS) in 1991, various free trade agreements (FTAs), and eventually the Eurasian Economic Union (EAEU) from 2015.

Third, the growth of China and Asia changed the world including Russia's trade, again with growing trade and another geographical turn of trade flows, this time towards China. From the turn of the century, the share of China in Russian imports increased dramatically, mainly at the expense of the CIS.

Fourth, Asia's growth contributed to commodity price hikes: from the turn of the century, commodity prices rose sharply for a whole decade, followed by a decade of strong fluctuations.³ For Russia, being one of the world's largest

¹ The figure is for trade in goods (export plus imports), based on data from the Slavic-Eurasian Research Center, Hokkaido University, Japan; see <https://src-h.slav.hokudai.ac.jp/database/SESS.html#USSR-S1>.

² COMECON was formed in 1949 as a response to the Marshall plan and the emerging Western European Integration. COMECON included the USSR, six European countries that are now part of the European Union (Poland, Czechoslovakia, East Germany, Hungary, Bulgaria, and Romania), and four other countries (Albania, Cuba, Mongolia, and Vietnam).

³ See <https://www.imf.org/en/Research/commodity-prices>.

commodity exporters, the changing terms of trade had a strong influence on the volume and patterns of trade.

In this chapter, we examine Russia's trade and trade policy in the light of these changing tides, leading up to the pre-war situation of early 2022, where increased geopolitical tensions, including the Russia-Ukraine conflict, and the green transition have been added to the trade agenda.

12.2 RUSSIA'S TRADE GROWTH DURING TRANSITION

After the collapse of the Soviet Union and the COMECON in 1991, the foreign trade of Russia exploded. Figure 12.1 shows the trade openness of Russia (exports plus imports as a share of GDP) during 1996–2020.

In 2021, Russia was a much more open economy than it was in 1989. After the initial rapid transition in the 1990s, the trade/GDP share has stabilised just below 50%. Hence, Russia is more open than large nations such as the United States (26% in 2019) or China (36%), but more closed than the majority of Western European countries (for example, Germany 88%, and France, Italy, and the United Kingdom in the 60–64% range).

While transition created a more open Russia, the country is still a relatively small trader in global comparison. The trade of Russia is much smaller than that of the United States and China, and smaller than the trade of medium-sized European nations such as Germany, France, the United Kingdom, and Italy. For example, the trade of Germany in 2018 was more than four times

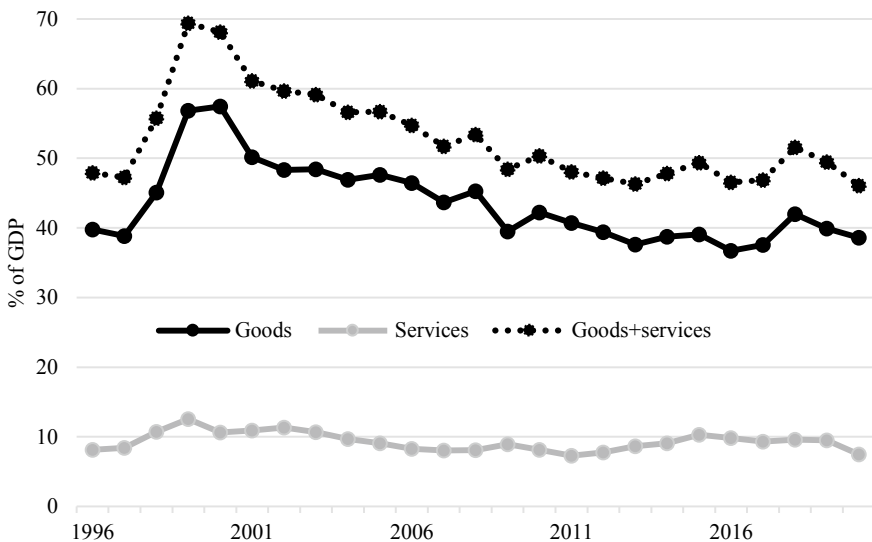


Fig. 12.1 Russia's foreign trade in % of GDP, 1996–2020 (Source World Bank's World Development Indicators)

that of Russia. For trade, therefore, Russia is not a superpower, but a medium-sized nation at par with Western European countries. This is revealed in Fig. 12.2, showing Russia's share of the world total for selected variables.

For trade in goods, Russia's trade is at par with its share in world nominal GDP, however with exports larger than imports, rendering a significant trade surplus. For trade in services, Russia is relatively larger, but this time with more imports than exports and a corresponding trade deficit.

Corresponding to Russia's massive land area, Russia has a very large share of total natural resource rents in the world economy (Fig. 12.2). This share has grown in the 2000s, illustrating Russia's role as a major commodity exporter in the world economy. This is a key feature of Russia's foreign trade and the reason for the sizeable trade surplus for goods in recent years.

Price fluctuations are generally stronger for commodity trade than for manufacturing, so we expect that Russia's fuel exports vary over time. But changing oil and gas prices do not only affect fuel trade, they also affect Russia's imports and non-fuel exports. This correlation between commodity trade fluctuations and other trade flows is quite strong for Russia. As an illustration, Fig. 12.3 shows nominal Russian exports and imports, with exports split into fuel and non-fuel, together with the commodity price index of the International Monetary Fund (IMF) during 1996–2020.

The influence of commodity price fluctuations is remarkable, with two of the trade curves following commodity prices like shadows. The correlation between fuel exports and the commodity price index is 0.99, so most of the variation in fuel exports is due to price changes. But Russia's imports were also strongly correlated with commodity prices, with a correlation of 0.94. For

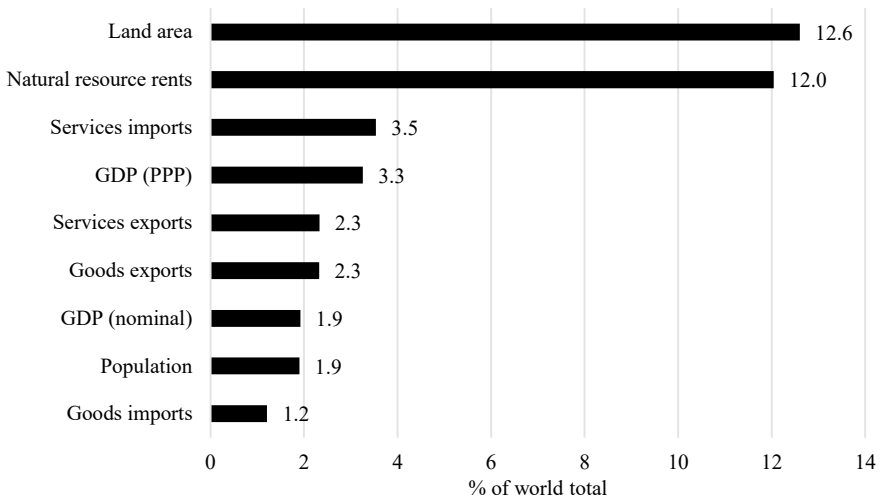


Fig. 12.2 Russia's share of the world total, 2018 (Source ITC trade map, World Bank's World Development Indicators)

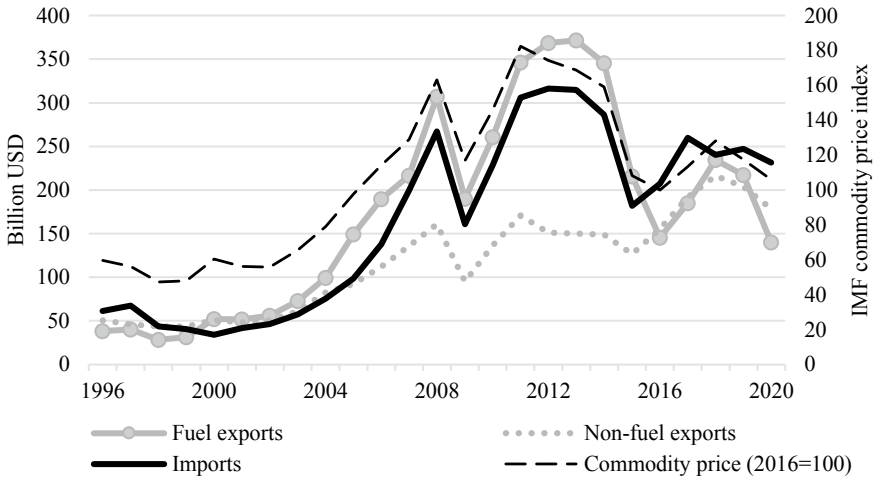


Fig. 12.3 Russia's trade versus commodity prices, 1996–2020 (*Sources* COMTRADE and IMF Commodity Price Index)

non-fuel exports, the development was less volatile, but still with a correlation of 0.76.

This co-variation may occur for different reasons: it may be due to a macroeconomic effect (commodity revenues allow more imports); value chain effects (upstream impact of changed commodity prices); or a 'spurious' correlation whereby commodity trade and other trade are affected by the same underlying shock. While an in-depth causal analysis is beyond the scope of this chapter, the persistence of the co-variation over time suggests that the macroeconomic mechanism may have been at work: commodity trade revenues were largely spent on importing. But the other causal mechanisms were of importance as well, for example, the global financial crisis (GFC) in 2007–2009 affected all trade flows. The exchange rate also played a role; the rouble rate dropped considerably from 2014, making imports more expensive and declining in dollar terms.

Figure 12.3 also reveals that during the 25-year period, Russia's trade experienced strong growth. This was partly driven by commodity prices and peaked around 2012. During the 2000s, Russian trade grew exponentially, with five-year moving growth annual averages of about 30% over several years. During this period, Russia's share of world trade increased (Melchior, 2018, 2019). This was followed by shrinking trade in the five-year periods ending from 2015 to 2018.

With rising oil prices, the share of fuels in Russia's exports of goods soared from 43% in 1996 to a peak level of 71% in 2012–2013. Even if this share dropped again to 44% in 2020, a continuous post-Soviet worry in Russia has been about diversification: Has Russia become over-reliant on fuels and

commodity exports, and how is this affected by trade policy? Will liberalisation lead to further deindustrialisation? These questions (see, e.g., EBRD, 2012 for a broad discussion) are important in Russia's trade policy debates.

12.3 RUSSIA'S WTO MEMBERSHIP

With memories of the centrally planned economy of the Soviet Union, the pro-communist opposition to President Yeltsin resisted liberalisation after 1991. The agricultural lobby and some oligarchs also supported the idea of building new industries sheltered from import competition (Aslund, 2010). Proponents of liberalisation and Russia's WTO membership, on the other hand, maintained that the WTO would guarantee market access abroad for non-oil exports, and thereby contribute to industrial diversification. According to this view, Russian exports of metals and other industrial goods might be subject to protectionist measures from other countries, unless protected by WTO rules. A study for the World Bank, however, suggested that less than one-tenth of Russia's gains from WTO membership would be due to better market access abroad: the largest gains would be due to domestic reforms, replacing former bureaucracies by new and modern institutions and regulations (Tarr, 2007). According to this analysis, such reforms would be particularly important for the services sectors.

Russian trade reform started in the 1980s in the perestroika period: some foreign trade operations were decentralised from 1988, and the Soviet Union applied for observer status in the General Agreement on Tariffs and Trade (GATT), normally a step towards membership. Observer status was approved by the GATT in 1990 (GATT, 1990). Russia became a member of the IMF (and the World Bank) in 1992, establishing a trade-friendly currency regime (current account convertibility). In 1993, Russia also applied for GATT membership, which widened to the WTO when it was established in 1995.⁴ While GATT accession procedures had been relatively easy in the past, the WTO established a more demanding process, where incumbent members made more stringent demands and negotiations were difficult. The process was especially demanding for Russia and China, due to their importance and non-market legacy. During this process, Russia had to negotiate bilaterally with about 60 of the WTO's members until membership was finally approved in 2012. This was a frustrating process for Russia, also re-fuelling domestic debates about the virtues of membership. But President Putin made WTO membership a top priority in 2000 (Aslund, 2010), and President Medvedev supported the final steps in 2012. Russia's WTO accession thereby took 19 years. In the WTO Trade Policy review of Russia (WTO, 2021, p. 32),

⁴ WTO included not only GATT but also General Agreement on Trade in Services (GATS), Trade-Related Intellectual Property Rights (TRIPS), and common institutional arrangements (on dispute settlement and notification requirements, among others).

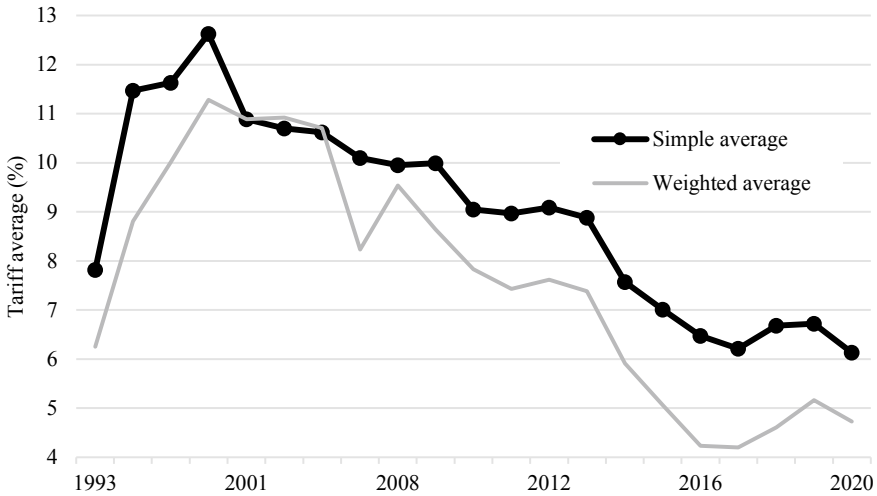


Fig. 12.4 Russia's applied tariffs, 1993–2020 (Source WITS/COMTRADE)

Russia's continuous unambiguous support for the global trading system is emphasised, in spite of some domestic reservations.

Figure 12.3 suggests that Russia's trade stagnated just after its WTO entry in 2012. But we have seen that commodity price fluctuations played a key role in this development. Disentangling the impact of WTO membership from other determinants of trade is not an easy task, in the presence of transition, Chinese growth, and more on top of commodity prices. Transition implied that liberalisation also took place independently from the WTO. Figure 12.4 shows that Russia's average tariffs⁵ also declined before Russia joined the WTO.

For WTO accession, Russia agreed to reduce average tariffs from 10 to 7.8%, immediately for some goods and with transition periods up to seven years for sensitive sectors (agriculture, automotive, and civil aircraft) (Tochitskaya, 2012). These tariff cuts were completed in 2020 and are reflected in Fig. 12.4.

Beyond tariffs, Russia committed to several reforms as part of the WTO package. In many institutional areas, Russian reforms took place during the 19-year WTO accession process, and it is not always easy to say what was due to WTO negotiations and what would have happened anyway. Some reforms also took a very long time—for example, the transition of Russia's veterinary control from the former 'prescriptive' regulations to a more modern

⁵ The figure shows the 'MFN', i.e., Most Favoured Nation, tariffs that apply to countries without any trade preferences. A technical issue is how to include so-called specific tariffs, i.e., tariffs of the form 'x roubles per kilogram' and the like; see Tarr (2007) for a discussion. In Fig. 12.4, we have used the 'UNCTAD method' available in the World Integrated Trade Solution (WITS) software.

risk-based approach as advocated by the Food and Agriculture Organization (FAO) (Black & Kireeva, 2015). This process started with WTO membership but continues 10 years after accession.

For trade in goods, the WTO agreement had several implications beyond tariffs. This e.g. included the following:

- Administration of tariffs was simplified;
- Product regulations such as veterinary standards would be subject to WTO rules;
- Russia was subjected to WTO rules for safeguard measures and duties against dumping or illegal subsidies.

Has Russia implemented these reforms as appropriate? A useful source in this respect is the trade policy reviews of the WTO, with the latest edition in 2021 (WTO, 2021).⁶

On tariff administration, Russia has improved its regime, now jointly with partners in the EAEU—see Sect. 12.5. Over time, there have been some WTO disputes on customs valuation. Recently, some concerns have been raised about digital product tracing systems established in 2019, potentially raising costs for traders (USTR, 2021).

Anti-dumping duties against imports at too low prices are frequently used by WTO members, particularly for ‘homogeneous’ goods where prices may easily be compared. Russia is a major exporter of such goods, for example, metals or fertilisers, and therefore subject to anti-dumping duties. Being subject to WTO rules was an advantage for Russia, not being treated as a ‘non-market’ economy any longer. Since 1995, Russia has been subject to anti-dumping measures by other countries 126 times, 37 of these in 2012 or later. At the same time, Russia imposed anti-dumping measures on other exporters 48 times, of which 30 were imposed in 2012 or later. For Russia, WTO membership improved the legal regime on anti-dumping and increased its own use of this trade remedy tool.

For veterinary standards and other product regulations, Russia has introduced important reforms, but there are still concerns among other WTO members. However, if one counts the number of complaints, Russia does not stand out as exceptional. If one counts the number of ‘specific trade concerns’ in the WTO Technical Barriers to Trade Information Management System, Russia received 24 complaints during 2012–2021, at the same level as the United States but much lower than China, India, and the EU.⁷ These complaints are often about domestic product regulations with an impact on

⁶ Other sources are the bi-annual reports on Russia by the US Trade Representative (the latest is USTR 2021) and the WTO trade monitoring reports on the G20 (see www.wto.org). Furthermore, the European Commission (2020) presents a comprehensive analysis of potentially trade-distorting practices in Russia.

⁷ See <http://tbtims.wto.org/en/SpecificTradeConcerns/Search>.

trade. In general, the impression is that for trade in goods, there are things to complain about in Russia, but Russia does not stand out as a particularly ‘bad’ case.

There are other areas, however, where the reach of Russia’s WTO membership is limited.

- Russia is not yet a member of the WTO’s agreement on public procurement, and recent reports indicate increased ‘buy Russian’ policies using national preferences in various forms. This applies to trade in goods as well as services.
- Based on measures of the Organisation for Economic Co-operation and Development (OECD) for trade in services, Russia has a relatively restrictive trade policy in this field. The OECD’s Services Trade Restrictiveness Index (STRI) estimates by sector indicate that Russia’s trade restrictiveness is above the average for most services sectors, compared to the 35 countries for which the STRI is calculated. The Russian regime has also become somewhat more restrictive in the second half of the 2010s.⁸ Three sectors stand out as particularly restrictive: rail freight transport, cargo-handling and storage, and storage/warehouse. Restrictions on foreign entry, barriers to competition, and the lack of regulatory transparency are key drivers behind the high STRI scores for these sectors. Services are often delivered through foreign affiliates, and restrictions on FDI therefore limit services trade. In recent years, Russia has generally tightened its FDI regime, limiting foreign access, including new ‘investment screening’ from 2017 (USTR, 2021; WTO, 2021).

On this basis, one may conclude that WTO membership led to important Russian reforms and liberalisation in some areas. But some trade barriers remain for goods, and the regime for FDI and services is more restrictive.

As noted earlier, the analysis of Tarr (2007) suggested that institutional changes in Russia would provide the most important benefits for Russia. The model-based analysis of Melchior (2018, 2019) suggests that multilateral trade integration of the WTO type leads to a welfare gain for Russia, mainly due to lower import prices. Interestingly, there is no deindustrialisation effect, and the benefits are rather evenly shared across Russian regions. Here, Rutherford and Tarr (2006) obtain different results, with the highest benefits in north-west Russia, St. Petersburg, and the Russian Far East. This is perhaps because they use a different type of model and account for the WTO impact on FDI in services. Hence, it is important to take into account FDI and domestic reforms, in addition to cross-border trade barriers.

⁸ See <https://www.oecd.org/trade/topics/services-trade/documents/oecd-stri-country-note-rus.pdf>. These STRI country notes are renewed every year and we refer to the version of January 2021.

12.4 RUSSIA'S BILATERAL AND REGIONAL TRADE AGREEMENTS

At the same time as Russia embraced globalisation and the WTO, it aimed to maintain strong ties with the FSU countries. The formation of the CIS in 1991 was the new platform, followed by a later 'spaghetti bowl' of various agreements with varying trade ambitions and mixed successes with respect to implementation. While the three Baltic states dropped off this wagon from the start, the other FSU countries joined, at least during the early stages.

The most successful track of integration in the FSU area has been the various steps leading to the formation of the EAEU in 2015; with no less than seven preceding agreements—the first dating from 1995 and the customs union implemented in 2010.⁹ The EAEU is a deep trade agreement, starting with Russia, Belarus, and Kazakhstan, and later joined by Armenia and Kyrgyzstan. The EAEU has a common external trade policy; it is currently the EAEU and not Russia alone that initiates new FTAs with third countries. The EAEU also has common trade legislation in an increasing number of fields, however with a tentative flavour in the sense that exceptions are allowed. For example, Kazakhstan had lower external tariffs than the common external tariff of the EAEU, and this is accepted, although temporarily, for more than one thousand tariff lines (WTO, 2018). The EAEU also develops common product regulations, for example, in the veterinary field, but many regulations are still national, and partners are allowed to introduce temporary national measures in some circumstances. Hence, the EAEU has not yet developed a binding common trade machinery like the EU, but it is on its way as the most successful trade agreement in the FSU and is an advanced trade agreement by global standards. While the ambition is broad, the focus so far is mainly on trade in goods, but the migration regime is also advanced by global standards (Vinokurov, 2017). The EAEU aims for a comprehensive internal market for goods, services, and investment, and allows labour migration between members. In terms of power relationships, the EAEU is probably more inequitable than the EU, where smaller countries have more influence, and no single nation can dominate. Armenia, Kazakhstan, and Kyrgyzstan had to accept almost doubling their external tariffs, since the common external tariff was set close to Russia's tariffs.¹⁰ Another exception to the united external policy is that the EAEU states have not agreed about Ukraine sanctions.

Russia hopes that more CIS countries and perhaps others may join the EAEU. Recently, observer status has been offered as an intermediate step, granted to Moldova (2018), Cuba, and Uzbekistan (2020).

Beyond the EAEU, in 2021 Russia had other FTAs in the FSU:

⁹ For a detailed overview, see WTO (2018).

¹⁰ According to Tarr (2016), the countries lose from this but could potentially gain from migration and the reduction of non-tariff barriers in the EAEU.

- An FTA with Georgia from 2001;
- The CIS FTA from 2013, including the EAEU countries plus Moldova, Tajikistan, and Ukraine¹¹;
- FTAs with Azerbaijan, Turkmenistan, and Uzbekistan from 2012–2013;
- Bilateral agreements with Belarus and Kazakhstan also remain in force.

Beyond the CIS, Russia concluded an FTA with Serbia in 2012. More recently, the EAEU has initiated joint FTAs with third countries, starting with Vietnam (2016) and followed by Iran (2019), Singapore, and Serbia (concluded in 2019, but not yet in force by late 2021). At the end of 2021, negotiations were ongoing with Egypt, India, and Israel.

On the whole, Russia's bilateral trade policies have had some achievements, but mainly in the FSU, with only a few FTAs beyond, and few major markets involved so far. Melchior (2018, Chapter 3) compares the coverage of FTAs between the 41 largest trading countries in the world (with the EU as one), and Russia comes out close to the bottom of this list.

12.5 THE GEOGRAPHY OF RUSSIA'S FOREIGN TRADE

Regarding the geographical composition of trade, Russia's point of departure in 1989 was that 61% of trade beyond the Soviet Union was with 'socialist countries', mainly COMECON, and about one-fourth with 'developed capitalist countries'. This changed rapidly with transition. We can distinguish two phases:

- Early transition, 1990s: Strong reallocation of trade from COMECON towards Western Europe and the rest of the world (ROW);
- From 2000: Strong reallocation towards China, particularly for imports and mainly at the expense of the FSU area.

Figure 12.5 shows the change during 1996–2020 (data for the early 1990s are not included in the COMTRADE database, perhaps because they are less reliable). Exports are split into fuel and non-fuel.

The main patterns are

- The FSU remains an important market for Russian non-fuel exports, but the FSU share of fuel exports declined in the 1990s and the share of the CIS in Russia's imports declined dramatically, especially during the 2000s and 2010s;
- After a decrease in the 1990s, the EU-28 has a continuously high share of Russia's foreign trade, especially fuel exports. A closer look reveals

¹¹ Russia revoked the FTA with Ukraine from 1 January 2016.

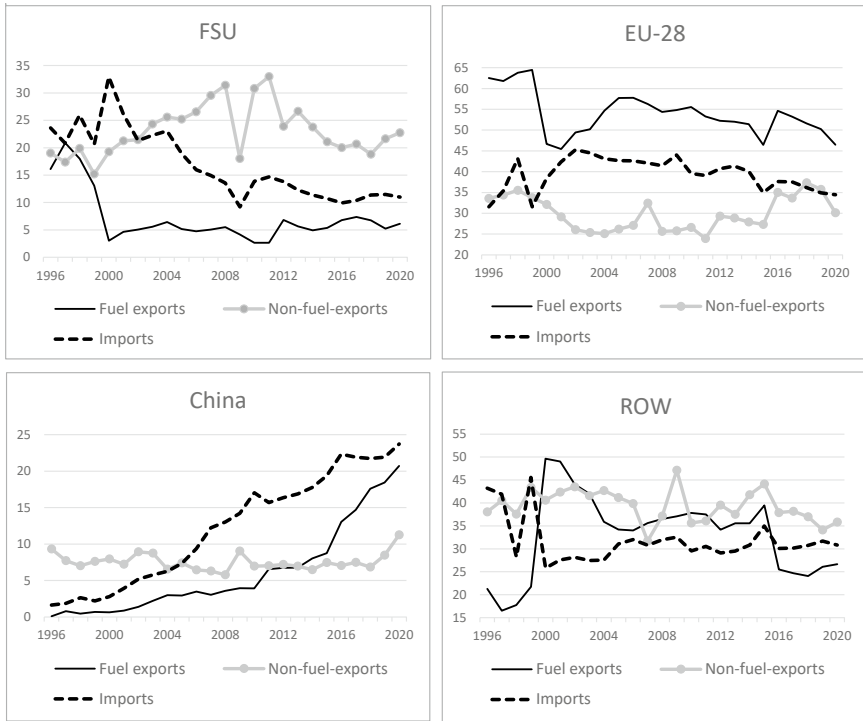


Fig. 12.5 The changing geography of Russia’s foreign trade, 1996–2020, % of Russia’s trade with all countries for each trade flow (*Source* WITS/COMTRADE)

- that the drop in the 1990s was particularly for the forthcoming new EU Member States (including Central Europe);
- There was spectacular growth in imports from China and fuel exports to China. China’s share of Russia’s imports grew from 1.6% in 1996 to 24% in 2020. The share of China in non-fuel exports was relatively stable, and much lower than for the FSU and EU-28;
 - The ROW had a significant share of about one-third of Russia’s trade, with some fluctuations. The United States and North America represent only a modest part of this, so Russia has extensive trade with many countries all over the world. Commodity trade tends to be more globally oriented than manufacturing trade (Melchior, 2018), and the extensive global trade of Russia is in line with this.

The analysis shows that the EU became Russia’s largest trade partner after 1991, but trade with China accelerated strongly from the 2000s and partly replaced Russia’s imports from the FSU area. This reallocation has continued also after the formation of the EAEU and other FTAs in the FSU area. While

China's growth is the main reason for this development, it is also evident that Russia's FTAs in the FSU area have not been able to reverse this trend.

We have already seen that fuel exports in the 2010s accounted for up to 71% of Russia's exports of goods (in 2012–2013). In Russia's trade with the EU-28 and increasingly with China, the exchange of fuel exports for manufacturing imports is the main component. Is Russia about to become deindustrialised, and a pure commodity exporter? Has trade policy failed to promote Russian manufacturing production?

A qualification to the questions above is that the non-fuel exports of Russia have not always declined in absolute terms; there was a significant decline during 1996–2002 but then very strong growth until the financial crisis. Later recovery followed, but there was again a strong setback in 2015, and then eventually some growth towards 2020.

Table 12.1 shows the composition of Russia's non-fuel exports during 1996–2020, split into main categories.

While ores and metals had a stable share and arms exports are more volatile, agricultural/food exports have recently increased considerably. Other non-fuel exports (various manufacturing sectors) were more hit by the GFC in 2007–2009 and COVID-19 in 2020; otherwise, the trend is not so clear.

On the whole, we are not able to conclude that there has been a massive deindustrialisation of Russia, even if the manufacturing trade balance has deteriorated over time, especially due to growing imports from China. For Russia, the EU and the FSU remain important markets also for non-fuel exports. A reason to worry, however, is the steep decline in FSU market shares in Russian imports. So perhaps other FSU countries have more reasons to worry.

For Russia in 2022, Western Europe and China are the major trading partners, not the FSU. The FSU is nevertheless still important to Russia, since a prospering neighbourhood is vital also for Russia's growth, and a prospering Russia is crucial for other FSU economies. Likewise, for the FSU countries, trade with Western Europe and China will be of key importance, with proportions depending on whether they are located more to the west (such as Belarus

Table 12.1 The composition of Russia's non-fuel exports, 1996–2020

<i>Year</i>	<i>Share (%) of Russia's non-fuel exports</i>					<i>Non-fuel % of total exports</i>
	<i>Food</i>	<i>Ores and metals</i>	<i>Arms</i>	<i>Other</i>	<i>Sum non-fuel</i>	
1996	3.1	17.7	30.9	48.3	100	56.9
2000	2.5	18.8	28.8	49.9	100	49.4
2005	4.2	17.4	27.3	51.1	100	38.2
2010	5.5	16.2	34.9	43.4	100	34.4
2015	12.6	16.4	13.3	57.7	100	37.0
2020	15.7	16.2	25.3	42.9	100	56.0

Source WITS/COMTRADE

and Ukraine) or to the east (Central Asia). The same geography applies inside Russia; Western Europe is top of the list for St. Petersburg, while Russia's Far East trades mainly with China. From a trade and growth perspective, neither Russia, Russian regions, nor FSU countries should be forced to choose between east and west, both doors should be open. In this light, it makes sense that the EAEU in their strategic plan have this dual approach: integration with China as well as with the EU (EAEU, 2020, p. 8). According to Melchior (2018, 2019), Russia has nothing to fear, in the sense that such integration will not only provide welfare benefits but also stimulate industrial diversification.

In this context, it should be recalled that while the growth of China has led to deindustrialisation in some countries, it has also been the main driver behind the commodity price increase of the 25-year period studied here. The model-based analysis of Melchior (2018, Chapter 7) suggests that commodity-producing countries and regions obtained among the highest welfare gains from China's growth, due to the terms of trade gain: getting cheaper industrial goods in return for more expensive commodity exports. On the other hand, this also caused manufacturing contraction and falling nominal wages in the same countries. Trade integration with China, on the other hand, is different from Chinese growth and may potentially lead to a welfare gain combined with higher nominal wages and re-industrialisation (Melchior, 2018). And preferential trade integration via FTAs with China and the EU will be better for industrialisation than multilateral free trade, according to this analysis (*ibid.*).

12.6 TRADE POLICY CHALLENGES IN THE EARLY 2020S: FROM SECURITY TENSIONS TO THE GREEN TRANSITION

The election of President Donald Trump in the United States in 2016 marked the end of a 30-year period of globalisation and liberalism in trade. Under President Trump, the United States introduced new protectionist measures, started a trade war with China, and partly blocked the dispute settlement system of the WTO.¹² At the time of writing (January 2022), the world trade system has not yet settled after this earthquake, the acceleration of FTAs across the globe has generally been put on hold, and the prospects of new WTO reforms are highly uncertain. A new feature of US trade policy under President Trump was its 'securitisation'—i.e., protectionist measures motivated by geopolitical and security reasons. For example, new steel and aluminium safeguard measures were introduced in 2018 for alleged security reasons, the trade war with China was geopolitically motivated, and investment screening and export controls were tightened for security reasons.

While Russia has been a rather innocent victim of some of President Trump's measures (notably the new barriers for steel and aluminium), it has a

¹² For extensive documentation of US trade policies under President Trump, see www.piic.com.

long history of geopolitics in trade, dating from the COMECON era and with Iran recently on the top of the FTA priority list. At the time of writing (January 2022), the Russia-Ukraine conflict is a major obstacle to Russia's trade integration with Western Europe. In addition to the sanctions and countersanctions (see Chapter 14), conflicts in the FSU are harmful to economic growth in the region, affecting Russia as well as the countries concerned.

A challenge for commodity-trading countries is the potential conflict between export industries and domestic consumers: Russian consumers would like to have cheap electricity, energy, and grains; but the exporters benefit from selling abroad at the highest possible prices. With cables, pipelines, and international trade, prices may be bid up to the benefit of exporters but to the detriment of consumers. An illustration is the growing integration of European energy markets, leading to electricity and natural gas prices far above normal levels towards the end of 2021.

Russia has several times used export restrictions as a method to separate export markets from domestic consumer markets, for example, for not only grains but also other commodities (WTO, 2021, p. 56ff). Russia is not alone; another example was provided in 2020, when several countries introduced export restrictions for medical equipment, including the EAEU. This also illustrates that supply shortages can also be a motive for export restrictions, not only a means to maintain lower domestic prices. Such measures are generally harmful to consumers abroad; they limit supply and bid up prices. For exporters, they can have ambiguous effects; quantity limitations may bid up export prices and generate rents, but outright export bans will force exporters to sell domestically at lower prices. Russia abolished several export restrictions as part of WTO accession, and export taxes for oil and gas have recently been reduced (see Chapter 9). The WTO generally aims to limit the use of export restrictions even if they are allowed in special circumstances, especially in the presence of critical shortages of food or other essential goods (GATT Article XI).

In the future, export restrictions may be an increasingly controversial issue, for the following reasons:

- The green transition may increase global electricity demand and bid up electricity prices, which are linked to energy markets in general. An illustration is the European debate in 2022 about the delayed opening of the Nord Stream 2 natural gas pipeline from Russia to the EU, and to what extent variations in the Russian supply of natural gas contributed to the EU's electricity price hikes;
- Supply shortages for rare commodities may become more common in the future;
- Climate change may affect agriculture unevenly and create food shortages in some regions.

Such developments may create incentives for the increased use of export restrictions and conflicts in the future.

There are also growing tensions about security-based restrictions (for exports or imports), where the line between legitimate security concerns and economic motives such as protectionism has been blurred under President Trump. In the previous era of liberal world markets, this did not generate many serious conflicts. However, there is the potential for more conflict in the future if GATT's security clause (GATT Article XXI) is used as a blanket waiver for protective measures. An interesting case was the WTO dispute between Russia and Ukraine, where Russia used this clause to stop transit trade from Ukraine through Russia, and Ukraine filed a WTO complaint. The WTO panel ruling in 2019 mainly supported Russia. Ukraine accepted the ruling and said it would not appeal.¹³ The case illustrates the important role of the WTO in trade conflict resolution.¹⁴

The infamous 2018 steel and aluminium tariffs of President Trump were also introduced for security reasons, and Russia plus a dozen other countries complained in the WTO at the end of 2021. Some (including Russia), but not all, introduced countersanctions.¹⁵ The common front by China, Russia, Western Europe, Canada, and Mexico in this case illustrates that the United States was the odd man out in that context.

While security-related sanctions are not examined in this chapter, President Trump's policies also illustrate that sanctions may also be used for protectionist purposes. A grey area is also when security concerns are legitimate, but their implementation is influenced by trade policy concerns. A case in question is Russia's import ban for agricultural goods from the United States, the EU, and other countries, which fits into Russia's import substitution policies that were introduced from 2014 (see Chapters 14 and 19).¹⁶ While subsidies are more important than import restrictions in this context, these policies also create a possible motivation for non-liberal trade policies at the sector level, including non-tariff barriers and resistance to liberalisation.

An emerging trade policy challenge is coming from policies aimed to prevent climate change. The green transition will raise costs for industries worldwide, and the EU has presented a proposal for the Carbon Border

¹³ See https://www.wto.org/english/news_c/news19_c/dsb_26apr19_c.htm.

¹⁴ In spite of this, Russia has—at the time of writing—not yet joined the initiative to create a parallel dispute settlement body while the United States is still blocking the appointment of new judges in the WTO system. This Multi-Party Interim Appeal Arbitration Arrangement was set up in 2020, and by early 2022, the EU and 24 other WTO members including China were members. But not yet Russia.

¹⁵ The countries that complained were Canada, China, the EU, India, Japan, South Korea, Mexico, New Zealand, Norway, Russia, Sweden, Chinese Taipei, and Turkey. Some complained about steel only, others for steel and aluminium. See www.wto.org for information.

¹⁶ See also European Commission (2020, Chapter 6) for information on import substitution policies.

Adjustment Mechanism (CBAM) (European Commission, 2021). The EU has, along with many other countries, introduced a carbon emissions trading (CET) system, whereby EU industries must acquire quotas to cover their CO₂ emissions. While CET quotas were initially allocated for free, they could be traded in the CET market, and allocation will become increasingly restrictive and lead to higher quota prices. This will raise the costs of EU producers, which risk losing out in competition with third-country producers that do not have to pay for their CO₂ emissions. CBAM intends to re-establish a ‘level playing field’ in the EU market by taxing imports with rates linked to the CET price, also taking into account CET systems in the exporting country. In early 2022, it is not yet clear when and how CBAM will eventually be implemented, and there are vivid debates about the issue in the EU itself and with its trade partners, including about its WTO compatibility. In the initial proposal, the sectors covered were electricity, iron and steel, aluminium, cement, and fertilisers. These represent a small share of EU imports but a large share of CO₂ emissions. CBAM is particularly important to Russia because of its exports to the EU of metals and fertilisers.

Another key issue for Russia with respect to the green transition is the role of oil and natural gas. Cutting consumption of oil and natural gas would be a heavy blow to Russia, the Middle East, Norway, and other fuel exporters, and a core issue in debates about energy transition and climate change. While the world as a whole is not ready for such a step in 2022, CO₂ pricing will also affect demand in the near future. Given that the EU is the main customer for Russian fuel exports, EU policies in the field will be important. An important sub-issue is whether natural gas will be considered as a legitimate component of the green transition in the EU: for example, by replacing energy from coal. At the time of writing, the EU Commission has presented new proposals related to the so-called ‘taxonomy’ on which sectors are considered ‘environmentally sustainable’. The draft proposal added nuclear energy and natural gas to the list, subject to certain conditions.¹⁷ However, this is controversial in some corners, and the political outcome on the issue will be important for Russia’s trade in the future.

Questions for Students

1. What were the main changes in Russia’s foreign trade regime from 1985 to 1995?
2. In what way is it true that commodity price changes have been a major driver for Russia’s foreign trade during 1995–2020?
3. What were the main consequences of Russia’s WTO membership (list some of these)?

¹⁷ See European Commission press release 1.1.2022: EU Taxonomy: Commission begins expert consultations on Complementary Delegated Act covering certain nuclear and gas activities. https://ec.europa.eu/commission/presscorner/detail/en/ip_22_2.

4. What does it mean that the EAEU is a customs union with common external trade policies?
5. Is competition from China a threat to Russian manufacturing production and diversification?

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