

# The impact of conflicts on trade and goods turnover

## Free trade: the lost opportunity of unresolved conflicts

Political intolerance in the South Caucasus continues to restrict the integration process of the region, significantly impeding the economic development of the regional countries, whereas established trade relations could have seriously promoted the process of conflict resolution and stability in the region. Unfortunately, this is an opportunity that remains yet to be realized. A possibility of a direct trade between Armenia and Azerbaijan is excluded. Trade of goods made in Armenia even through third countries is immediately politicized and persecuted in Azerbaijan. The latter is even barring the calls from Armenia. Turnover of goods with Turkey is officially channeled through third countries. Opportunities of trade with Iran are jeopardized by international embargo on trading with the latter. Interrelated issues of free trade and political intolerance are particularly unique in the political and economic relations between Armenia and Turkey.

## Economic development of the region held hostage to Turkey's political goals

A number of facts such as the absence of diplomatic relations between Armenia and Turkey, the pro-Azerbaijani bias of Turkey in the process of conflict resolution in Nagorno Karabakh, the denial policy regarding the Genocide of Armenians in the Ottoman Empire and the issue of border recognition, the absence of direct economic relations, and roads and railway communication between the two countries, Armenia's blockade and embargo by Turkey, including the bans on importing goods of Armenian origin into the territory of Turkey and on transportation of goods to Armenia through Turkey, aim at specific goals: resolution of the NKR conflict in favor of Azerbaijan, prevention of the international recognition of the Genocide and recognition of the current border of Turkey. In the result of such a policy, Armenia, with the 85% of her borders being blockaded, continues to suffer economic loss. Meanwhile, the eastern regions of Turkey (located in historical Western Armenia) equally suffer economically.

## The reality of asymmetric trade opportunities

Still, there is some trade going on between the two countries, via the territories of Georgia and Iran. The indirect trade, though requiring increased costs, still shows a growing tendency. Incidentally, it is the annual import of goods from Turkey to Armenia that keeps increasing, comprising about 270 million USD in 2008, whereas the negligent volume of export from Armenia to Turkey is shrinking. There are flights from Istanbul to Yerevan. According to various sources, it is estimated that around 15 thousand Armenians work in Turkey, thus contributing to the development of the economy in this country. Another interesting fact: there is no restriction of any kind regarding Turkish goods in Armenia. In practice even financial transactions are being carried out among individuals from the two countries with the mediation of foreign banks. In general, the current policy of Turkey towards Armenia is rather asymmetric: it is directed against export of goods from Armenia, whereas export of Turkish goods to Armenia is not restricted in any significant manner.

## Lost opportunities

The business community in Turkey as well as the political authorities in the eastern provinces are interested in cooperation with Armenian partners, one of the goals of such cooperation being unmediated export of certain products such as cement, mineral resources and fish from Armenia. Direct import of specific Turkish products to Armenia may decrease the associated costs. Import quota on Turkish textile specified for the European community make Armenia attractive for the

Turkish investors, since there are no such restrictions in our country. Another factor making Armenia attractive for Turkish investors is the comparatively higher taxes on production and sale of certain products in Turkey, which makes the prospect of organizing such production in Armenia more attractive than importing these products. According to the findings of a recent 2010 World Bank study, the business environment in Armenia is more attractive for business investments due to certain features. Further deregulation and improvement of the business environment in Armenia will increase the competitiveness and attractiveness of this environment for the business people in the neighboring country. Certain services offered by the Armenian market, such as health and educational services, are of higher quality and are more affordable for the residents of the eastern provinces of Turkey.

### **Uncertain future**

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However, the prospects of free trade in the region are as vague and unpredictable as the future of conflicts resolutions. Opinions are contradictory. Some business people believe that liberalization of trade in case of the unresolved conflict will create new challenges. The 'ifs' are countless. There is a counterargument that free turnover will provide more beneficial conditions for freight and passenger transportation, will simplify the trade between the two neighboring countries, will boost the economy in Armenian regions bordering with Turkey, will promote healthier competition in the Armenian market and will enhance the productivity of Armenian producers. Yet others think that in the case when large regional transit projects are non-existent, it is simplistic to anticipate any significant economic benefits. Concerns are many: food safety and quality issues regarding imported products, inflation in real estate market and abated affordability of mortgage, legislative gaps in the regulation of foreign investment, Turkey's asymmetric trade policies favoring exports to Armenia vs. importing Armenian goods. While some believe that more competitive Turkish produce will flood our market and the Armenian producers will not be able to survive the race with import, others think that our market is already saturated and there is no any such threat. There are alerting concerns about the possible decay of the Armenian agriculture and the risk of depriving farmers of their lands. Some are rather skeptical about the prospect of exporting Armenian products into Turkish market. In case democratization process in Iran progresses, economic sanctions against this country will be removed and in the result, Iran's policy to protect its economy by strictly limiting import will be changed. Thus, its market will become more accessible for the export of Armenian goods.

### **Individual response to each situation**

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Uncertainties veiling the promotion of free trade under the conditions of unresolved conflicts and their possibly huge impact on the resolution of conflicts and stabilization of the region necessitate the need for a profound and extensive scenario building exercise, in order to respond to the possible developments and clarify their consequences and political feedback. The latter should be adequate to each situation: definition of strict schemes for the taxation of Turkish imported products, phyto-sanitary and quality certification, implementation of direct and indirect restrictions, supervision of the entry of Turkish capital into Armenia and the economic activities of Turkish business people, application of quality control mechanisms to the imported goods and protection of customer rights, provision of state support to the local producer, indirect subsidization of agricultural and processing industries, implementation of a protectionist policy regarding state purchases, promotion of European standards in the managerial practice in Armenian businesses, provision of state support to exporters to Turkish and European markets and so on.

*The paper is elaborated based on the opinions passed by the participants of the discussion "Realities of Armenian-Azerbaijani and Armenian-Turkish Business Relationship: Potential, Desire and Conflicts in Region", which took place on May 12, 2010. The roundtable discussion was attended by independent analysts, government officials, and representatives of the international organizations.*

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