



STRENGTHENING CONNECTIONS AND BUSINESS SYNERGIES BETWEEN TURKEY AND ARMENIA Towards a Roadmap for Confidence Building Through Economic Cooperation

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TEPAV conducted a fact-finding mission to Yerevan between November 11 and November 14, 2013. Twenty-five meetings were held with a variety of non-governmental organizations, think-tanks and research institutes, multilateral institutions and business people—including the VIP Tourism & Narekavank Tourism Agency—the Union of Manufacturers and Businessmen of Armenia (UMBA), Noyan Natural Juice Factory, Union of Information Technology Enterprises, Apaven Co. LTD, EV Consulting, the World Bank Group, International Center for Human Development, TOSP Knitting Factory, Caucasus Research Resource Center Armenia (CRRC), Armenia Institute of Tourism, Analytical Center on Globalization and Regional Cooperation, Public Journalism Club, National Competitiveness Foundation of Armenia (NCFA) and USAID.

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Executive Summary

In the past two decades, relations between Armenia and Turkey have been left in diplomatic limbo. The Armenian-Turkish border has been closed since 1993, which has been a major blow to the economic prospects of the region, among other things. Armenia's closed border with Turkey (as well as Azerbaijan) have limited the landlocked country's territorial connections to the Georgian and Iranian routes, while the border cities on the Turkish side suffer from the absence of economic activity in the region and are amongst the least developed regions in Turkey. The absence of official diplomatic relations between Armenia and Turkey makes a compelling case for the need to strengthen economic cooperation in order to help build confidence between the two countries. While the establishment of diplomatic relations and the opening of the land border remain the most pressing issues in the long run, strengthening cross-border business interactions can generate short-term results.

Against this backdrop, this report examines opportunities for cooperation in order to help facilitate economic interactions between Armenia and Turkey. Confidence-building measures and projects that are proposed in the final chapter of the report have been formulated based on research findings and results presented in Chapter 3 including (1) General Economic (macro-level) Diagnostics, (2) Product (micro-level) Assessment, (3) Sector (meso-level) Assessment, and (4) Policy Framework and Institutional Background. Key findings were used to identify critical opportunity areas in Chapter 3.5, *Synthesis of Results: A Taxonomy of Opportunities*.

The results of the General Macro-level analysis (Chapter 3.1) reveal the low level of economic activity in both Eastern Turkey and Armenia when compared to Turkey as a whole. Turkey's economy is almost twelve times larger than countries in the South Caucasus combined, while Armenia's economy is the smallest in the region. However, in spite of its low GDP and income per capita level, Armenia's human development index is slightly higher than that of Turkey. Armenia's high quality physicians and qualified ICT workforce—built on the strong math and science foundation established during the Soviet era—also demonstrates this point. The product micro-level assessment (Chapter 3.2) points to low trade complementarity between Armenia and Eastern Turkey. Also, given that the closed border further restricts trade of goods in the region, the chapter concludes that, in the short run, trade in services is the most viable form of economic cooperation between Armenia and Eastern Turkey. The next chapter (3.3 Sector (meso-level) Assessment) evaluates a selection of service sectors in both countries and the potential for bilateral cooperation. The sectoral analysis is complemented with an assessment of the policy context and institutional framework in both countries (Chapter 3.4).

In order to identify the final set of target sectors for cross-border economic cooperation, the preliminary list of sectors (in Chapter 3.3) are evaluated based on the following criteria: (i) The effect of the closed border on business interaction in the sector; (ii) The compatibility of the sector with Armenia's policy priorities; (iii) The compatibility of the sector with Turkey's policy priorities; (iv) Suitability of the sector for SMEs i.e., by assessing barriers that prevent firms from entering the sector. The evaluation revealed that the ICT, and the tourism and hospitality sectors present the most significant opportunities for business interaction between the two countries. Education, health, and retail sectors are also suitable for cross-border cooperation; however, opportunities for SMEs in these sectors are limited. Similarly, the energy and finance sectors require high-level capital investment and therefore are also not SME friendly. The possibility for cooperation in the transport and logistics sector is limited because of the closed border.

The final chapter of the report (Chapter 4) includes project ideas to facilitate business synergies between the two countries in the ICT and tourism sectors. The project ideas aim to build *confidence* between the Armenian and Turkish businesses as well as other critical stakeholders, such as the two countries' private sector support organizations, bureaucracy and political leadership. The final list of selected project ideas were also evaluated based on their political feasibility, technical correctness, and institutional capacity and include:

- *Impact Analysis for New Flight Routes,*
- *Joint Industrial Cooperation* (ICT value chain and market assessment),
- *Kars-Gyumri Special Tourism Zone around Ani,*
- *Utilizing multilateral platforms*

Placed within the broader context, the study identifies the most promising areas for economic cooperation in the South Caucasus and lays down the groundwork for more detailed research into specific sectors. As Track I diplomacy is expected to stall in the run-up to 2015, the continuation of all other efforts to increase cross-border cooperation in non-political and non-controversial areas is critical.

1 Research Background and Introduction

Today, the South Caucasus remains divided by conflicts, blockades, and border restrictions. While Armenia, Georgia, and Azerbaijan emerged as independent states after the dissolution of the Soviet Union, conflict quickly ensued in the region. Georgia entered a period of civil war that included inter-ethnic conflict between Georgian-Ossetians in South Ossetia (1988-1992) and Georgian and Abkhazians in Abkhazia (1992-1993), as well as clashes in Tbilisi that resulted in a coup d'état. At the same time, inter-state fighting broke out between Azerbaijan and Armenia over the disputed area of Nagorno-Karabakh. Armenia continues its blockade of Nachivan and of the unrecognized but de facto independent Republic of Nagorno-Karabakh while the Azeris continue to block road, rail, and energy links with Armenia

Turkey pursued a far more assertive foreign policy with its neighbors with the end of the Cold War: attaching particular importance to the Caucasus and the Central Asian countries where it has strong cultural and historical ties. While Turkey supported the independence of all the former Soviet Republics including Armenia, it sided with Azerbaijan as the Nagorno-Karabakh military conflict intensified in 1993, blocking trade with Armenia by closing its border with this country. The Turkish-Armenian border has also remained closed.

There have been various attempts to normalize relations between Armenia and Turkey, including the opening of the common border. Most notably, the signing of the *Protocol on establishment of diplomatic relations* and *Protocol on development of mutual relations* between Armenia and Turkey in 2009 offered a modicum of hope to bring the diplomatic deadlock between the two countries to an end. The first protocol covered the establishment of diplomatic relations and opening of borders, while the second focused on the further development of bilateral relations by forming an intergovernmental body that will be comprised of several sub-commissions (See Box hereunder). However, the diplomatic thaw between the two countries did not last long and the protocols were never ratified due to domestic political pressures on both sides.

Sub-commissions proposed under the *Protocol on development of mutual relations*

- the sub-commission to *conduct regular political consultations between the Ministries of Foreign Affairs of the two countries;*
- the sub-commission on transport, communications and energy infrastructure and networks to *make the best possible use of existing transport, communications, and energy infrastructure and networks between the two countries, and to undertake measures in this regard;*
 - the sub-commission on legal matters to *develop the bilateral legal framework in order to foster cooperation between the two countries;*
 - the sub-commission on science and education to *cooperate in the fields of science and education by encouraging relations between the appropriate institutions as well as promoting the exchange of specialists and students, and act with the aim of preserving the cultural heritage of both sides and launching common cultural projects;*
- the sub-commission on trade, tourism and economic cooperation to *take concrete measures in order to develop trade, tourism, and economic cooperation between the two countries;*
- the sub-commission on environmental issues to *engage in a dialogue and reinforce their cooperation on environmental issues;*
- the sub-commission on the historical dimension to *implement a dialogue with the aim to restore mutual confidence between the two nations, including an impartial scientific examination of the historical records and archives to define existing problems and formulate recommendations, in*

which Turkish, Armenian, as well as Swiss and other international experts shall take part.

Among other things, the closed border situation has been a major blow to the economic prospects of the region. Armenia's border problems with Azerbaijan and Turkey have limited the landlocked country's territorial connections to the Georgian and Iranian routes. Also pointing to the absent economic activity in the region, the border cities on the Turkish side are amongst the least developed in Turkey.

The absence of official diplomatic relations between Armenia and Turkey make a compelling case for the need to strengthen economic cooperation in order to build confidence between the two countries. Cross border economic cooperation can contribute to economic development and prosperity on both sides of the common border, as well as promote regional stability. An economic cooperation agenda was also part of the *Protocol on development of mutual relations in 2009*, which included plans to establish a separate sub-commission "to develop trade, tourism and economic cooperation between the two countries." While the establishment of diplomatic relations and the opening of the land border remain the most pressing issues in the long run, strengthening cross-border interactions between the local private sectors of the two countries can generate short-term results.

Against this background this report proposes a roadmap towards building trust and confidence based on identifying and facilitating mutually beneficial economic opportunities between Armenia and Turkey. Achievements in the economic realm are expected to follow progress on the more sensitive political issues. The research was guided by five main objectives that can be summarized as follows: (1) A bottom up approach emphasizing the role of local private sector for regional development; (2) Increasing cross-border interaction; (3) Empowering SMEs in the region through strategic interventions; (4) Enlarging public and political support for economic interaction; (5) Ensuring sustainable economic growth in the region.

The results of the research are presented under four main headings: (1) General Economic (macro-level) Diagnostics; (2) Product (micro-level) Assessment; (3) Sector (meso-level) Assessment; (4) Policy Framework and Institutional Assessments. The research is based on statistics collected from national and international databases, a literature review, and findings and interviews from fieldwork in Armenia.

Key findings were then used to identify critical opportunity areas in (Chapter 3.5) *Synthesis of Results: A Taxonomy of Opportunities*. In order to identify the final set of target sectors for cross-border economic cooperation, a preliminary list of sectors were evaluated based on the following criteria: (i) The effect of the closed border on business interaction in the sector; (ii) The compatibility of the sector with Armenia's policy priorities; (iii) The compatibility of the sector with Turkey's policy priorities; (iv) Suitability of the sector for SMEs, i.e., by assessing barriers that prevent firms from entering the sector. The evaluation revealed that the ICT and the tourism and hospitality sectors present the most significant opportunities for business interaction between the two countries.

The final chapter of the report (Chapter 4) includes project ideas to facilitate business synergies between the two countries in the ICT and tourism sectors. The project ideas aim to build *confidence* between the Armenian and Turkish businesses as well as other critical stakeholders, such as the two countries' private sector support organizations, bureaucracy, and political leadership. The final list of project ideas that were selected were also evaluated based on their political feasibility, technical correctness, and institutional capacity. The projects are divided

into three principal types depending on the aim and method: 1) Interaction and connectivity projects; 2) Feasibility studies and; 3) Advocacy projects and Capacity building projects.

Placed within the broader context, the study identifies the most promising areas for economic cooperation, laying down the groundwork for more detailed research into specific sectors. As Track I diplomacy is expected to stall in the run-up to 2015, the continuation of all other efforts to increase cross-border cooperation in non-political and non-controversial areas is critical.

2 Methodology

This section introduces the methodological tools and conceptual framework of the study. First, we introduce the main objectives guiding the research process as well as the identification of the research location. Then we provide a detailed description of the methodological tools used to collect data and information, which are presented under four main headings: (1) General Economic (macro-level) Diagnostics; (2) Product (micro-level) Assessment; (3) Sector (meso-level) Assessment; (4) Policy Framework and Institutional Assessments.

Main Objectives

The purpose of this research is to explore business opportunities and projects that can enhance economic cooperation and synergies in the South Caucasus, as well as contribute to the rapprochement process between Turkey and Armenia. Main objectives include enhancing the role of local private sector, increasing cross-border interactions, empowering SMEs in the region, enlarging public and political support for economic interaction, and ensuring sustainable economic growth in the region. The main objectives guiding the research process are detailed as follows:

- (1) **A bottom-up approach that emphasizes the role of the local private sector in each country to boost regional development.** The study aims to explore bottom-up ways for local private sectors to apply their resources and capabilities in the regional marketplace to trigger regional development in the short run. In this respect, the study focuses on underdeveloped regions, namely Eastern Turkey and Armenia. Turkey's eastern regions are the poorest in the country and Armenia has the lowest GDP per capita in the South Caucasus region. Under-development in both regions is partly due to inter-regional connectivity problems, as the mountainous Eastern Anatolian region is far from the economic and logistical hubs of Western Turkey, while landlocked Armenia has closed borders with two of its neighbors (Turkey and Azerbaijan). Solving these problems requires political breakthroughs and large-scale economic investments in the long run. In the meantime, taking advantage of local resources and capabilities is an important short-term strategy for enhancing growth and expanding employment in the region. Thus, the identification of key local resources and capabilities were important considerations in the selection of sectors and products examined by this study.
- (2) **Increasing cross-border interactions.** The project aims to create sustainable links between Armenian and Turkish businesses and people, with an emphasis on borderland regions. Cross-border relationships between Armenia and Turkey have been constrained for over two decades due to conflicts in the South Caucasus. The closure of borders between Armenia and Turkey as well as between Armenia and Azerbaijan hampered regional economic and cultural interactions, which in turn reinforced the region's economic woes. Today, there is very little civil society interaction between Armenian actors/organizations and their counterparts in Eastern Turkey, with Armenian NGOs often instead working with their counterparts in Istanbul.⁵ Hence, this study emphasizes intra-regional economic cooperation on the Turkish-Armenian borderlands in order to demonstrate the benefits of cross-border cooperation.
- (3) **Empowering SMEs in the region through strategic interventions:** SMEs are the main drivers of job creation, growth, and economic diversification. Moreover, they have local roots and

⁵ Cuhadar and Punsmann 2012

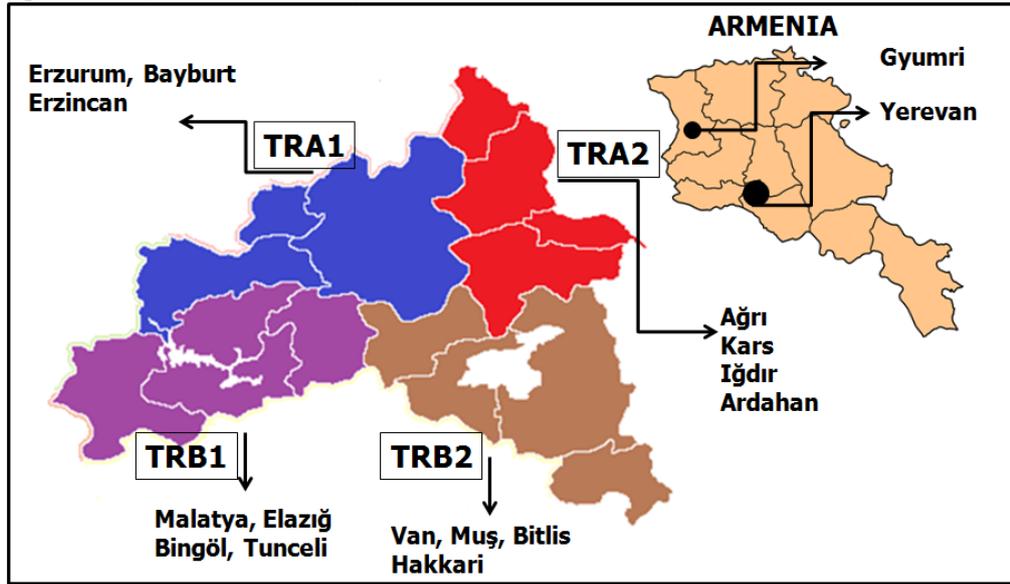
provide local jobs. Therefore, robust and sustainable regional growth depends on empowering SMEs. For this purpose, the study first examines possibilities to support SMEs in spreading their activities beyond national borders. At present, SMEs face several constraints on making investments abroad, outsourcing their activities, and sometimes even exporting their products. Addressing challenges such as language and logistical barriers will help SMEs cooperate with a wider spectrum of companies in the region and take advantage of complementarities in areas including marketing and technology. Moreover, businesses on both sides of the border will increase their value-added output and market access, and therefore thrive. Secondly, the study also seeks to identify new sectors and products that are suitable for SMEs. Diversification of SMEs into new business areas will strengthen their presence in the region.

- (4) **Enlarging public and political support for economic interaction.** The benefits of economic cooperation are manifold and can, therefore, garner the necessary public support to increase interaction between the two countries. Access to the Armenian market (considering Yerevan is the largest city in region that is located to the east of Gaziantep), and Armenia's links to the Commonwealth of Independent States (CIS) countries, provide important opportunities for Eastern Turkey. In turn, capital inflows as well as technical know-how from Turkey can help Armenia diversify its economy, improve its competitiveness, and boost employment. In addition to a macro level regional cooperation analysis, the study identifies specific sectors and products that can help boost growth and employment in the region.
- (5) **Ensuring sustainable economic growth in the region.** The key findings in this report yield a set of project ideas for further research, and recommendations that aim to improve economic productivity and interaction in the region. Increased productivity is key for long-term economic growth in both countries. Therefore, the study emphasizes that financial and human resources be allocated to sectors and value chains that create the highest added value and reach markets with the highest potential. Projects that build on the region's existing economic potential and on complementarities between regional actors can facilitate continuous cross-border investment and trade.

Research Location

The main geographical focus of the study is Armenia and the eastern regions of Turkey bordering Armenia. In the General Economic (macro-level) Assessment, the eastern regions of Turkey, classified according to *nomenclature d'unités territoriales statistiques* (NUTS) at level 2, are TRA1 (Erzurum, Bayburt and Erzincan Provinces), TRA2 (Ağrı, Kars, Iğdır and Ardahan Provinces), TRB1 (Malatya, Elazığ, Bingöl and Tunceli Provinces), and TRB2 (Van, Muş, Bitlis and Hakkari Provinces). For the Product-level Assessment the eastern regions of Turkey, classified according to NUTS at level 1, are TRA region (includes TRA 1 and TRA2) and TRB region (includes TRB1 and TRB2).

Figure 1 Map of Eastern Turkey and Armenia



The study also makes comparisons between Armenia and Turkey at the national level, where appropriate, and where NUTS 2 level data is not available. Comparisons with Georgia and Azerbaijan have also been made in some sections in order to provide a wider regional perspective. The different data that has been used throughout the study is explained in greater detail in the *Layers of Assessment*, hereunder.

Layers of Assessments

The results of the research are presented under four main headings: (1) General Economic (macro-level) Diagnostics; (2) Product (micro-level) Assessment; (3) Sector (meso-level) Assessment; (4) Policy Framework and Institutional Assessments. The research is based on statistics collected from national and international databases, a literature review and findings, and interviews from fieldwork in Armenia. A variety of analytical tools have been used, some of which are already well established in the literature, and others developed by TEPAV specifically for this study. Units of analysis (e.g. country, region, province, sector, product group, firm etc.) varied depending on different analytical tools that were used throughout the study and the availability of data. The methodological and analytical tools that have been used in each section are as follows:

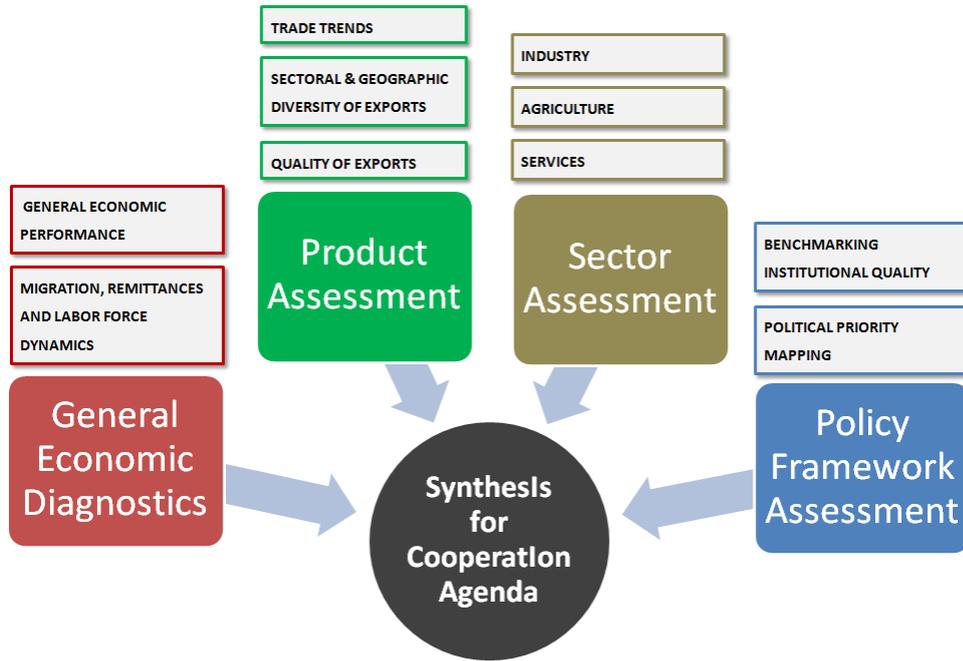
- (1) **General Economic (macro-level) Diagnostics:** The General Economic (macro-level) Diagnostics examines economic structures and recent economic and sectoral trends in countries in the South Caucasus region, and in Turkey based on statistics taken from national and international databases. The Armenian and Turkish (both national as well as NUTS 2 regions') economies were compared based on their overall performance as well as on a selection of macro-level, development, and demographic indicators. Macro-level, development, and demographic data for Georgia and Azerbaijan were also used in some instances in order to provide a wider regional perspective. Moreover, the section provides sectoral breakdowns and migration data for Armenia and Eastern Turkey (TRA and TRB). Data for FDI flows and remittances were only available at the national level for Turkey.

- (2) **Product (micro-level) Assessment:** This section puts trade patterns into perspective at the product level. First, the section compares trade volumes of Turkey and Armenia with their respective neighbors. Second, an in-depth analysis of import and export structures of Armenia and Eastern Turkey's TRA and TRB regions has been carried out. Armenia and Eastern Turkey's regions' (TRA and TRB) level of export diversification were examined using several diversification indicators. The quality of Turkish and Armenian exports were calculated based on EXPY⁶, which measures the productivity level of exports. The Trade Complementarity Index (TCI) was also used to identify trade complementarities between Armenian and Turkey's TRA and TRB regions.
- (3) **Sector (meso-level) Assessment:** For the sectoral assessment a preliminary list of sectors were evaluated including the construction, tourism, ICT, healthcare, agro-food, and textile and apparel sectors. This section includes the assessment of services sectors, which are not included in the Product Assessment. The analyses of services sectors are based largely on qualitative data (on literature reviews and insights collected during interviews), as comparable quantitative data for the two countries was limited—albeit international, regional, and sectoral reports and databases also provided quantitative statistics. The aim of the sector assessment was to identify possible synergies (i.e., market access and skills complementarity) that can arise from further economic interaction between Armenia and Turkey.
- (4) **Policy Framework and Institutional Assessment:** This section assesses recent economic policies as well as the overall policy environment and institutional structure in the region with a focus on Armenia. Most of the insights presented in this section were gathered during the fact-finding mission to Yerevan in November 2013 from interviews with stakeholders, development agencies, and local chambers. The section also includes a *policy priority mapping* of flagship government policies affecting the private sector, as well as public sector initiatives and projects that influence competitiveness. Government policies and strategies discussed include Armenia's Export-Led Industrial Policy, EurAsEc Customs Union membership, and *Open Skies* policy, as well as Turkey's most recent Five-Year Development Plan and regional development policies of Turkey's eastern regions. The **Policy Framework and Institutional Assessment** provides a broader understanding of the context that complements the macro, product, and sector level analyses (that are largely quantitative). It also assesses the political feasibility of economic cooperation by identifying risks and opportunities under the current policy frameworks of the two countries.

Key findings were then used to identify critical opportunity areas in *Synthesis of Results: A Taxonomy of Opportunities*. In order to identify the final set of target sectors for cross-border economic cooperation, a preliminary list of sectors were evaluated based on the following criteria: (i) The effect of the closed border on business interaction in the sector; (ii) The compatibility of the sector with Armenia's policy priorities; (iii) The compatibility of the sector with Turkey's policy priorities; (iv) Suitability of the sector for SMEs, i.e., by assessing barriers that prevent firms from entering the sector. The evaluation revealed that the ICT and the tourism sectors present the most significant opportunities for business interaction between the two countries. The final chapter of the report (Chapter 4) includes project ideas to facilitate business synergies between the two countries in the ICT and tourism sectors.

⁶ Hausmann, Ricardo & Hwang Jason & Rodrik, Dani, 2006.

Figure 2 Framework of the Study



3 Main Findings and Results

3.1 General Economic (macro-level) Diagnostics

Background

In the past decade, both the Armenian and Turkish economies grew rapidly. Both countries have experienced boom-boost cycles although Turkey—which has been relatively more engaged in global markets compared to Armenia—was less vulnerable to external shocks than Armenia.

While it was an important manufacturing center of the region during the time of the Soviet Union, Armenia's double-digit growth performance in the 2000s was driven by high rates of private transfers to the construction sector, which accounted for one-third of GDP⁷. During this period, Armenia did not develop competitive industries and improve its access to global markets. The investment-led growth model in the unproductive construction sector suffered a major setback in 2009, shrinking by 14.2%. In recent years, the Armenian government has been seeking a new paradigm to replace the fragile construction-based economic growth.

The Turkish economy, on the other hand, improved its productivity markedly in the 2000s.⁸ The country has more competitive industries, and it has been more engaged in global markets compared to Armenia. This is also partly due to its customs union with the European Union since 1995, which granted free access to the EU markets (and vice versa) for industrial goods⁹. The 2001 Turkish economic crisis led to significant macroeconomic reforms, which also gave a major impetus for growth during the 2000s. Turkey was hit by the global economic crisis in late 2008, albeit it recovered quickly. However, short-term capital flows, heavy reliance on energy imports, and the crisis in the Eurozone (Turkey's main trading partner), are making the Turkish economy vulnerable to external shocks.

Moreover, Turkey faces a serious challenge, related to regional imbalances in productivity and income per capita. Similar to Armenia, Turkey's eastern regions are landlocked, and the already low number of industrial sectors and high dependence on public spending presents very few opportunities for growth in these regions. The Turkish government has taken various measures in the past few years to channel investments to underdeveloped regions, including the Regional Investment Incentives Scheme specifically directed towards regional development that provides benefits to companies investing in underdeveloped regions.

Overall Economic Performance

The Turkish and Armenian economies differ in terms of size and income. While Turkey's economy is almost twelve times larger than the economies' of the South Caucasus countries combined, Armenia's USD 10 billion economy makes it the smallest in the South Caucasus. Similarly, Turkey's GDP per capita level is the highest in the region while Armenia's is the lowest—

⁷ World Bank, 2013a

⁸ *The Economist* 2012, April 7

⁹ Also, starting with 1980, Turkey moved from import substitution to export-oriented growth, gradually lifted trade barriers, removed subsidies and adopted a more flexible exchange rate policy.

at about one-third of Turkey's. Turkey has a low poverty rate of 4.7% at USD 2 per day, while the poverty rate in Armenia is roughly four times higher.

Table 1: Selected macro-level indicators for Armenia, Azerbaijan, Georgia and Turkey

	Nominal GDP, billion \$, 2012	GDP per capita, 2012, \$	2002-12 GDP per capita growth (const. 2005 \$)	Poverty ratio at \$2 PPP a day, 2010
Armenia	9.9	3,337	99%	19.9%
Azerbaijan	68.7	7,227	207%	2.8*%
Georgia	15.8	3,508	81%	35.6%
Turkey	789.3	10,666	43%	4.7%

*:2008 data

Source: World Bank

In terms of size, Armenia's economy is similar to the eastern regions of Turkey. Armenia's GVA in 2010 was USD 8.3 billion, comparable to the TRB1 region, which has a USD 8.9 billion economy. Armenia's GVA per capita decreased significantly after the 2009 crisis, falling to USD 2,801, which is lower than all the eastern regions of Turkey. Remittances slightly increase Armenia's gross national income to USD 3,300 in 2010 and USD 3,720 in 2012.

Figure 3: GVA of Armenia and Eastern Anatolian regions in 2010, million \$

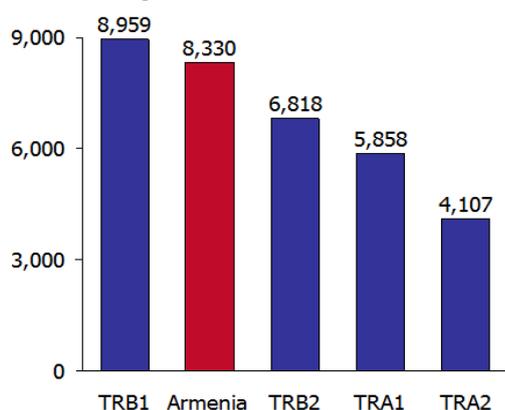
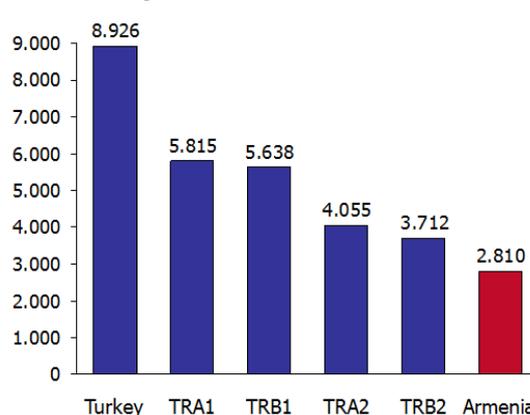


Figure 4: GVA per capita of Armenia and Eastern Anatolian regions in 2010, \$



Sources: TUIK, World Bank, TEPAV Calculations

Development

According to the United Nation's Human Development Index, Armenia and Turkey have similar development levels: ranking 87th and 90th out of 187 countries and territories, respectively. Armenia fares slightly better in terms of health and education indicators while Turkey's GNI per capita is more than double compared to Armenia's.

The two countries have the same level of life expectancy of about 74 years. According to the HDI, the two countries have similar scores for health, while Armenia's capacity in terms of institutional capacity and healthcare personnel (measured by hospital beds and physicians per 1000 people) is much higher than Turkey. On the other hand, the infant mortality rate of Armenia is significantly higher than in Turkey.

The Armenian population's mean years of schooling and gross secondary enrollment rate are higher than that of Turkey, although Turkey performs better on the expected years of schooling indicator.

Turkey's GNI per capita at USD 13,710 is more than double the amount for Armenia. Lastly, the car ownership rate in Armenia, a proxy for middle class size, is higher than the eastern regions of Turkey but lower than Turkey's national average.

Table 2: Selected Development Indicators, 2010-2012

	TRA1	TRA2	TRB1	TRB2	Armenia	Turkey
HDI Value (UN, 2012)					0.729	0.722
HDI Rank (UN, 2012)					87 th	90 th
Life Expectancy (UN, 2012)					74.4	74.2
Infant Mortality Rate (per thousand)	10.2	15.4	17.1	11.4	14.7	12.2
Hospital beds per 1000 people, 2010	3.7	1.4	3.6	1.9	4.0	2.5
Physicians per 1000 people , 2005-2010					3.7	1.5
Adult literacy rate (% ages 15 and older), 2005-2010					99,6	90,8
Mean years of schooling (UN, 2012)					10.8	6.5
Gross secondary enrollment, 2010-11	89%	64%	108%	65%	92%	82%
Expected years of schooling (years) (UN, 2012)					12.2	12.9
GNI per capita (2005 PPP USD) (UN, 2012)					5540	13710
Motor vehicles per 1000 people , 2010-11	66	23	69	20	103*	155

*2007 Data

Sources: World Bank, UN, TUIK

Demographics and labor force

Armenia is demographically similar to eastern Turkey in terms of population size and level of urbanization, but has a higher labor force participation rate and an older median age.

The combined population of Turkey's eastern regions is slightly above Armenia's population. Armenia is more urbanized than all of its neighbors in the South Caucasus except for Turkey. Moreover, Armenia's capital Yerevan, home to more than 1.1 million people, hosts as high as 58% of the country's population. Yerevan is the largest city east of Gaziantep that is close to Eastern Turkey, and the third largest in the Caucasus after Baku (2.1million) and Tbilisi (1.2 million).

Although Armenia has a relatively small workforce compared to its neighbors, it's labor force participation rate is moderately higher than its neighbors, especially Turkey's rate. Labor force participation in the eastern regions of Turkey is even lower than the national average, with the exception of TRA2.

Armenia also has a relatively old population, with the country's median age higher than all its neighbors except for Georgia. Moreover, the median age for Turkey's eastern regions are particularly low compared to the national average.

Table 3: Selected demographic indicators for Armenia, Azerbaijan, Georgia and Turkey

	Population in millions, 2012	Share of urban population	Labor force, millions, 2011	Labor force participation rate	Median age
Armenia	3.0	64.2%	1.4	64.1%	32.9
Azerbaijan	9.3	53.9%	4.6	69.6%	29.8
Georgia	4.5	53.0%	2.4	68.1%	39.6
Turkey	74.0	72.3%	26.6	52.9%	29.2
TRA1	1.0	63.3%	0.3	48.4%	26.7
TRA2	1.1	48.7%	0.3	55.0%	22.2
TRB1	1.6	67.6%	0.6	50.0%	28.7
TRB2	2.0	50.0%	0.5	45.8%	20.2

Sources: World Bank, CIA World Factbook, TÜİK

Main industries and sectoral indicators

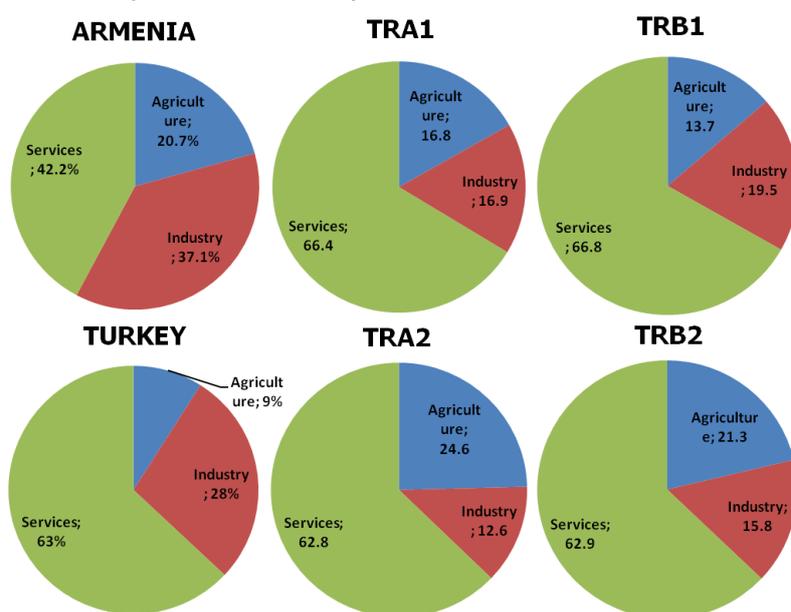
In Armenia the GDP share of industry and agriculture is high, while the share of services sector is low compared to Turkey; the high share of agriculture in the Armenian economy resembles some eastern Turkish provinces.

Armenia is an industry-oriented economy, with the sector's GDP contribution as high as 37.1%, compared to 28% in Turkey. The high contribution of industry to GDP, however, is largely due to Armenia's large mining and energy sectors, while the manufacturing industry's GDP contribution is as low as 10.7%, compared to 19.5% in Turkey.

The contribution of services is much larger in the Turkish economy compared to its contribution to the Armenian economy. The share of services in GDP passes the 60% mark for all eastern regions compared to 42% in Armenia. In fact, some eastern provinces have a larger share of services sector than the Turkish national average. Lack of connectivity to markets reinforces the absence of industrial production in these regions where the main economic activity is in the low-level services sector.

With respect to the share of agricultural production, Armenia resembles Eastern Turkey where the sector represents a major portion of local economies. In Turkey the regions in the eastern part of the country are less industrialized and the shares of agricultural as a share of GDP are more than double or triple the national average. The agriculture sector in Armenia is the largest sector in terms of added value followed by retail and construction. However, the large shares of agriculture production in Eastern Turkey and Armenia's GDPs do not mean that their agriculture sectors are competitive.

Figure 5: Compositions of GDP by Sector, 2012



Sources: World Bank, TUIK

A look at the corporate sector: Size and activity

Armenia's economy is dominated by large firms. The contribution of SMEs to the employment share in Armenia was only 42% in 2012, compared to 78% for Turkey.^{10 11}

The top three enterprises in Armenia and Eastern Turkey are in the energy, mining, and utilities sectors, and in the cement, textile, and mining sectors, respectively. Combining the Armenia and Eastern Anatolia economies, the dominant industries are food and beverages, mining, and metals. The latter two (mining and metals) industries require high capital investments, pointing to difficulties in linking SMEs to regional supply chains.

Table 4: Top 10 Taxpayers of Armenia in 2012

Rank	Company Name	Sector
1	Zangezur Copper-Molybdenum Factory	Metals
2	ArmRos Gazprom	Energy
3	K-Telecom	Telecom
4	Alex-Grig	Trading&Retail
5	Armen Tel	Telecom
6	Flash	Energy
7	City Petrol Group	Energy
8	Armenian Electricity Networks	Utilities
9	Dine Gold Mining Company	Mining
10	Avers	Trading

Source: Armenia State Revenue Committee

¹⁰ OECD, 2013a

¹¹ OECD, 2013b

Table 5: Largest Companies in Eastern Anatolia by Net Sales, 2012

National Rank	Company Name	City	Sector
168	Aşkale Çimento Sanayii T.A.Ş.	Erzurum	Cement
426	Eti Krom A.Ş.	Elazığ	Metals
531	ANATEKS Anadolu Tekstil Fabrikaları A.Ş.	Malatya	Textiles
804	Yurt Çimento San. ve Tic. A.Ş.	Muş	Cement
995	İlhan Tekstil San. ve Tic. A.Ş.	Malatya	Textiles

Source: Istanbul Chamber of Industry

Migration, Remittances and Labor Force Dynamics

Emigration has an important impact in both Armenia and Eastern Turkey, where large numbers of citizens emigrate in search of better economic opportunities. Since 1991 there has been a steady decline in the Armenian population.¹² A large number of Armenian citizens live and work in former Soviet Union countries such as Russia and Ukraine. According to the most recent data, 770 thousand Armenian citizens are living abroad: 517 thousand in Russia, 89 thousand in the USA, and 50 thousand in Ukraine.¹³ However, official migrant numbers only account for documented Armenian citizens, and do not include undocumented migrants from Armenia, some of whom are also living and working in Turkey.

Furthermore, there are members of the Diaspora without Armenian citizenship. Although Diaspora estimates vary, it is often cited that about 6 million Armenians live outside of Armenia (compared to Armenia's 3 million population). While Armenians emigrated to different countries and regions of the world throughout history, today's Armenian Diaspora was formed largely as a result of migration out of the Ottoman territories during the first war, and during and after the dissolution of the Soviet Union.

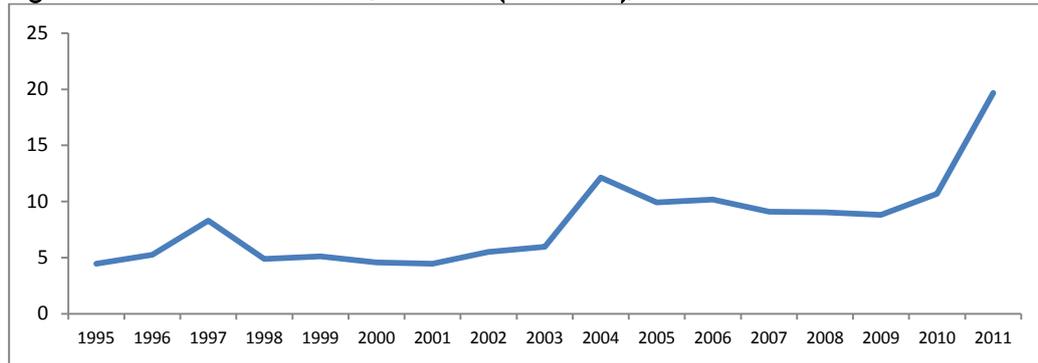
Remittances from workers abroad, which averaged 9.6% of the GDP between 2001 and 2011, constitute an important part of Armenia's national income. These remittances, channeled towards the real estate investments, were one of the key drivers of the construction boom of the 2000's. During this period, more than half of real estate purchases were estimated to be done by Armenian citizens living abroad, most of whom resided in Russia, which was the source of 72% of total remittances.¹⁴ Nevertheless, since these remittances could not be channeled into more productive and sustainable areas such as manufacturing or services, their long-term impact on economic growth is limited.

¹² World Bank; ILO 2009

¹³ United Nations Population Division 2013

¹⁴ OECD 2011

Figure 6: Personal remittances, received (% of GDP), 1995 – 2011



Source: World Bank

Eastern Turkey is one of the least populated areas of Turkey, yet it still suffers from large-scale migration to western regions. Turkey’s eastern regions have high emigration rates comparable to those of Armenia, with TRA having the highest proportion of its residents moving out of the region. In 2012, the difference between numbers of people engaged in inward and outward migration from both areas was -61,425, which accounted for a net loss of 1% of the total population. Nevertheless, there is a trend towards lower population loss due to migration in TRA and TRB, where the net migration rates increased from -2.6% and -1.0% to 1.5% and 0.7%.

Figure 7: Migration Statistics of Eastern Turkish Regions, 2012

Region	Population, 2012	Inward migration	Outward migration	Net migration	Net migration rate (per thousand)
TRA	2.226.155	63.300	97.734	-34.434	-15,35
TRB	3.756.322	112.229	139.320	-27.091	-7,19

Source: Turkish Statistics Institute

Istanbul, Eastern Marmara, and the Aegean regions are the main destinations of people emigrating from Eastern Turkey. In 2012, 70 thousand out of 237 thousand émigrés from Eastern Anatolia chose to move to Istanbul, which is the commercial and industrial center of the country. The Eastern Marmara region, one of the most important manufacturing centers of Turkey, received 28 thousand migrants from the eastern region, while the Mediterranean and Aegean regions each received around 27 thousand. Eastern Anatolian migrants predominantly choose coastal areas, where the services sector provides employment opportunities for low-skilled workers. Although the Central and Western Anatolian regions are also emerging manufacturing centers in Turkey, these are less popular migration destinations.

Table 6: Emigration from Eastern Turkish Regions by Destination, 2012

		TRA	TRB
	Turkey	97.734	139.320
TR1	İstanbul	29.082	40.671
TR2	Batı Marmara	5.461	5.749
TR3	Ege	12.567	14.685
TR4	Doğu Marmara	14.773	14.084
TR5	Batı Anadolu	10.168	12.322
TR6	Akdeniz	6.020	20.945
TR7	Orta Anadolu	3.635	5.044
TR8	Batı Karadeniz	3.593	4.019
TR9	Doğu Karadeniz	4.778	2.604
TRA	Kuzeydoğu Anadolu	-	5.225
TRB	Ortadoğu Anadolu	4.571	-
TRC	Güneydoğu Anadolu	3.086	13.972

Source: Turkish Statistics Institute

Concluding Remarks for General Economic (Macro-level) Diagnostics

Size of economy. Turkey's economy is almost twelve times larger than the economies of the South Caucasus countries combined. Armenia's economy is the smallest in the region.

Income per capita. Turkey's has the highest GDP per capita in the region, while Armenia is the poorest country, with income per capita levels at roughly one-third of Turkey's. Armenia's GVA per capita decreased significantly after the 2009 crisis, dropping below all eastern regions of Turkey. Remittances slightly increased Armenia's gross national income

Development indicators. According to the United Nation's Human Development Index, Armenia and Turkey have similar development levels. Armenia fares slightly better in terms of health (except for the infant mortality rate indicator) and education indicators while Turkey's GNI per capita is more than double compared to Armenia. The car ownership rate in Armenia, a proxy for middle class size, is higher than the eastern regions of Turkey but lower than Turkey's national average.

Demographics. Armenia is demographically similar to Eastern Turkey in terms of population size and level of urbanization, and it is more urbanized than all of its neighbors in the South Caucasus (except for Turkey). The capital Yerevan is the largest city east of Gaziantep that is close to Eastern Turkey—pointing to opportunities for the tourism sector among other services offered in urban areas. However, Armenia's median age is higher than all its neighbors (except for Georgia), while the median age for Turkey's eastern regions are particularly low (even compared to the national average).

Labor Force. Armenia has a small workforce compared to its neighbors, although its labor force participation rate is moderately higher, especially than Turkey's participation rate. Labor force participation in the eastern regions of Turkey is even lower than Turkey's national average.

Main industries and sectoral indicators. In Armenia the GDP share of industry and agriculture is high, while the share of services sector is low compared to Turkey. The high contribution of industry to GDP is largely due to Armenia's large mining and energy sectors, while the

manufacturing industry's GDP contribution is low. The contribution of services is much smaller to the Armenian economy compared to its contribution to the Turkish economy and to the eastern regions of Turkey (for the latter, high share of services in GDP is due to the absence of industrial production in these regions, where the main economic activity is in low-level services sector). The high share of agricultural production in GDP in the Armenian economy resembles some Eastern Turkish provinces and is indicative of low-level of connectivity in the landlocked regions that reinforce the absence of industrial production.

Size and activity of the corporate sector. Armenia's economy is dominated by large firms and the contribution of SMEs to employment is much lower compared to that of Turkey. In terms of sector activity, dominant industries in both Armenia and Eastern Anatolia are food and beverages, mining, and metals. The latter two (mining and metals) industries require high capital investments, pointing to difficulties in linking SMEs to regional supply chains.

Migration dynamics. Emigration has an important impact on both Armenia and Eastern Turkey, where large numbers of citizens emigrate in search of better economic opportunities. Since 1991 there has been a steady decline in the Armenian population due to emigration to former Soviet Union countries such as Russia and Ukraine. In addition to official migrants there are undocumented migrants (some of whom are also living and working in Turkey) and a large Armenian Diaspora without Armenian citizenship. Emigration rates in Turkey's eastern regions, one of the least populated areas of Turkey, are comparable to those of Armenia. The wealthier western regions of Turkey—including Istanbul, Eastern Marmara, and the Aegean regions—are the main destinations of people emigrating from Eastern Turkey. Eastern Anatolian migrants predominantly choose coastal areas, where the services sector provides low-skill employment opportunities, while the Central and Western Anatolian regions, also emerging manufacturing centers, are less popular migration destinations

Remittances from Armenian workers. Remittances from Armenian workers abroad that were channeled towards the real estate investments in Armenia were one of the key drivers of the construction boom in the 2000s, and they continue to constitute an important part of Armenia's national income today. Nevertheless, since these remittances could not be channeled into more productive and sustainable areas such as manufacturing or services, their long-term impact on economic growth is limited.

The general macro-level assessment points to the low level of economic activity in landlocked Eastern Turkey and Armenia. While links to economic centers (including Western Turkey) are promising, regional collaboration and coordination is key for Armenia and eastern Turkey to improve their economic conditions. The synergies between Armenia and Turkey / Eastern Turkey need to be identified in order to further cement the economic cooperation and deepen regional integration. The next section will, therefore, evaluate trading structures and patterns of Turkey and Armenia, and the possibility of increased trade cooperation between them.

3.2 Product (micro-level) Assessment

The product (micro-level) assessment focuses on trading structures and patterns of Turkey and Armenia. We first evaluate trade trends of Turkey and Armenia with their neighbors, Georgia, Bulgaria and, Azerbaijan. We also compare Eastern Turkey and Armenia in terms of trade volume over time and their top trading partners. In addition we also look at the qualities of exports and trade complementarities between Armenia and Eastern Turkey. The main findings from these analyses are presented below.

As Turkey's geographic and economic size is much larger and diversified than that of Armenia, we will look at specific regions of Turkey, particularly eastern provinces, which border Armenia. According to NUTS1 geographic classification there are 12 regions in Turkey¹⁵, and we will focus on Turkey's eastern regions TRA (North-Eastern Anatolia) and TRB (Middle-Eastern Anatolia) in order to benchmark trade data. In order to calculate trade patterns, we took aggregated data for each eastern province of Turkey and Armenia using the Harmonized System (HS) at the six-digit level. In addition, we also used bilateral (province-to-country) trade data for Turkish provinces at the HS two-digit level.

We used disaggregated bilateral trade flow data provided by the United Nations Statistical Division, which is available in the UN Commodities Trade Statistics Database (COMTRADE). Although COMTRADE is the most comprehensive database on world trade, it does not capture certain trade flows. Many countries do not report on time, and some countries report data compiled at too high a level of aggregation to accurately capture sectoral activity. Moreover countries' import and export volumes are not consistent with each other as discrepancies can be found when comparing a country's exports with its corresponding partner's import flows. In order to address some of these problems, we complemented COMTRADE data with the BACI (Base pour L'Analyse du Commerce International – Database for International Trade Analyzes) database for the product assessment analyses. The BACI database offers values for trade data to a higher degree of disaggregation in product (more than 5,000 products) and spatial (more than 200 countries) dimensions. Furthermore, the BACI database corrects discrepancies found between one country's exports and its corresponding partner's import flows. The BACI dataset has been particularly useful for the TRA and TRB regional analyses.

Overall Trade Trends

Turkey has strong economic relations with its neighbors Georgia and Azerbaijan in the South Caucasus and Bulgaria in the Balkans. In the following analysis of we included Bulgaria—which is about the same size as Azerbaijan and is also a post-Soviet country—for illustration purposes; in contrast with South Caucasus countries, Bulgaria is an EU member state. In 2012 Turkey was ranked the number one export partner of Georgia, the number one import partner of Azerbaijan, and was listed among the top 10 trade partners of all its neighbor countries. Armenia is the only country in the region that Turkey does not have strong economic relations with. Turkey's share in Armenia's exports is very low, although 5.6% of Armenia's total imports come from Turkey.

Table 7: Top import partners of Azerbaijan, Bulgaria and Georgia 2007-2011 average.

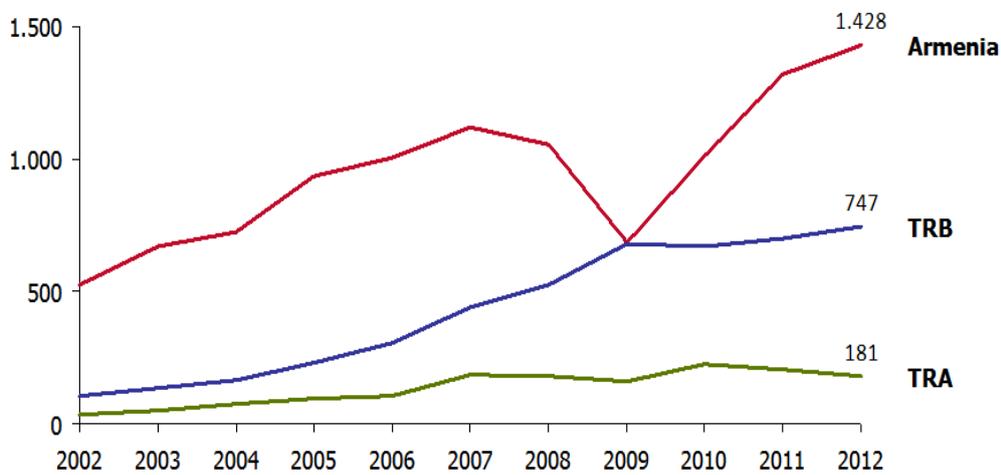
Azerbaijan		Bulgaria		Georgia	
Import Partners	Share	Import Partners	Share	Import Partners	Share
Russia	16.8	Russia	14.4	Turkey	15.9
Turkey	14.1	Germany	10.9	Ukraine	9.4
Germany	8.4	Italy	6.6	Azerbaijan	8.3
China	7.6	Turkey	6.2	Russia	7.2
Ukraine	7.0	Romania	6.1	Germany	6.7

Source: BACI, Comtrade, Tepav Calculations

¹⁵TurkStat Classification Server

In addition to being a landlocked country, Armenia’s economic interactions in the region are limited due to the closure of two of its borders. Armenia has tried to overcome the negative effects of low cross-border trade by using air freight. In 2012 Armenia’s average export distance was 3719 km while Turkey’s average export distance was 2846 km.¹⁶ Armenia’s ability to send products to farther destinations is also reflected in its large export volume compared to its neighbor regions TRA and TRB, which are also geographically constrained. In 2012 Armenian exports were double the size of TRB’s export volume and almost eight times larger than Turkey’s TRA region. All three regions saw their export volume grow since 2002; amongst the three regions, Armenia’s exports experienced the sharpest decline after the crisis but recovered rapidly after 2009. TRB’s export volume has also been rising in the past decade, albeit at a much slower pace. TRA’s export volume on the other hand, has remained low and relatively stable since 2009.

Figure 8: Exports of Armenia, TRA and TRB, USD million



Sources: TUIK, Comtrade, TEPAV Calculations.

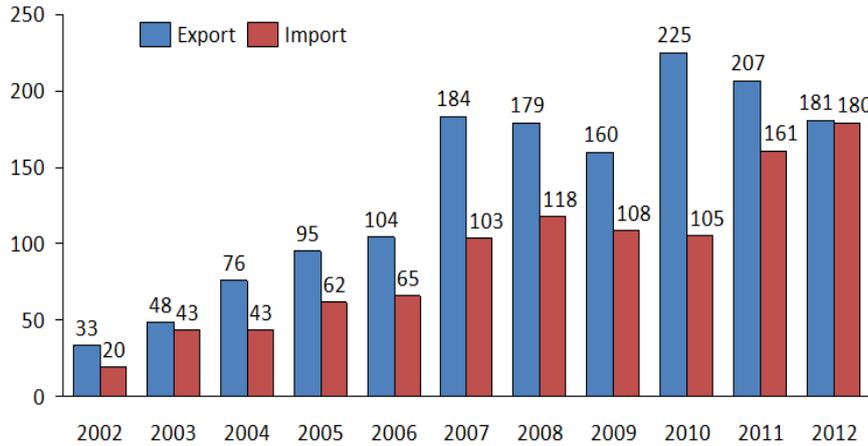
While Armenia’s exports increased rapidly, so have its imports, accounting for the country’s growing trade deficit. The TRB region, on the other hand, runs a trade surplus and the TRA region’s export and import volumes are almost equal. The following three sections take a closer look at each region’s export and import patterns.

TRA Region

Both exports and imports of the TRA region have been increasing over the past decade. Exports of the region increased six fold from USD 33 million to USD 181 million between 2002 and 2012. The TRA region’s exports peaked in 2010 after the global crisis. In the past ten years, the export surplus in the region was driven by iron and steel exports, which increased from USD 15 million to USD 35 million between 2002 and 2012. In 2012 the region’s imports caught up with its export volume, and the region’s trade surplus has narrowed down significantly. Moreover, most imports of Turkish regions are registered in Istanbul or other major port cities, and trade figures may not reflect TRA region’s actual trade balance.

¹⁶ Export volume weighted average distance between reporter and partner country.

Figure 9: Exports and Imports of TRA, USD million



Source: TUIK

The TRA region exports 804 different types of products. Azerbaijan receives the major share of the TRA region's exports, followed by Iran and Ukraine. Given Azerbaijan and Iran's significant share in the region's exports (85% of total export in 2012), the TRA region's average trade distance was relatively short at 1577 km. On the other hand, the TRA region's major import partners were distant countries such as China and Germany, but also including nearby Iran. The TRA region's top three import partners account for almost 50% of its total imports.

Table 8: Top Export and Import Partners of TRA Region, 2012

Country	Exports, USD million	Country	Imports, USD million
Azerbaijan	111	China	44,8
Iran	41,9	Germany	28,5
Ukraine	3,5	Iran	21,9
Turkmenistan	3,4	Russia	20,5
Georgia	3,2	Uzbekistan	17,0
Russian Federation	2,8	Italy	5,1
Iraq	2,2	France	3,5
Hungary	2,1	Afghanistan	3,4
Uzbekistan	1,7	Egypt	3,1
Mozambique	1,6	India	3

Source: TUIK, TEPAV Calculations.

Table 9: The TRA Region's Top Ten Export Sectors, 2012

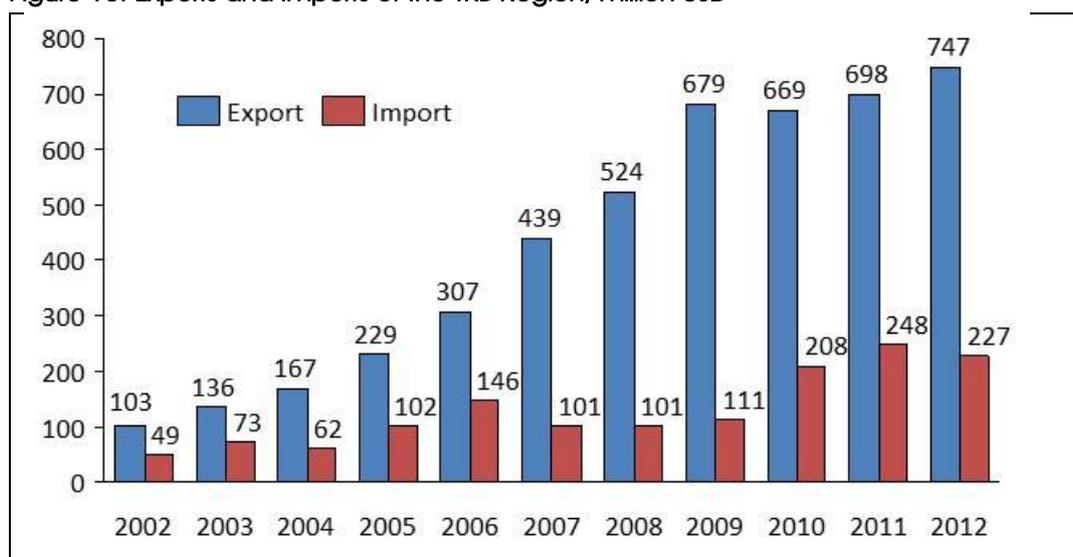
Sector Name	Exports, million USD
Iron and steel	35,2
Articles of iron or steel	29
Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	24,4
Wood and articles of wood; wood charcoal	19,6
Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	18,3
Plastic and articles thereof	13,9
Electrical machinery and equipment and parts thereof; sound recorders and reproducers,	10
Tanning or dyeing extracts; tannins and their derivatives; dyes, pigments and other	8,5
Furniture; bedding, mattresses, mattress supports, cushions and similar stuffed furnishings	7,8
Ceramic products	6,8
TOTAL	181

Source: TUIK, TEPAV Calculations.

The TRB Region

The TRB region's exports increased six-fold during the last ten years. In 2012, the export volume of the region reached its highest level, standing at more than triple its import volume. Export surplus in the region is driven by increase in the production of edible fruits and nuts, and peels of citrus fruit or melons. In the last decade, exports from these sectors increased by USD 115 million, and iron and steel exports increased by USD 90 million.

Figure 10: Exports and Imports of the TRB Region, million USD



Source: TUIK, TEPAV Calculations.

The TRB region exports 1864 different types of products. The region's main export partners are Iran, Iraq, and the Russian Federation, which account for 60% of the region's exports. Although

nearby Iran and Iraq are important export markets (55% of total export), the TRB region's average export distance was 2323 km in 2012 relatively higher than the TRA region's average export distance of 1577 km. This is due to the fact that the TRB region also exports goods to geographically distant countries such as China and USA. The region mainly exports edible fruit and nuts, peels of citrus fruits or melon fruit, and iron and steel.

Table 10: Top Export and Import Partners of the TRB Region, 2012

Country	Exports, million USD	Country	Imports, million USD
Iran	313,4	UAE	19,4
Iraq	98,2	Germany	18
Russian Federation	34,6	Tajikistan	16,3
USA	32	Italy	14
China	28,5	Iran	13,6
Germany	26,2	China	12,7
UAE	19,1	USA	12,2
France	13,8	Russia	10,4
Macedonia	13,8	India	10,2

Source: TUIK, TEPAV Calculations.

Table 11: TRB Region's Top Ten Export Sectors, 2012

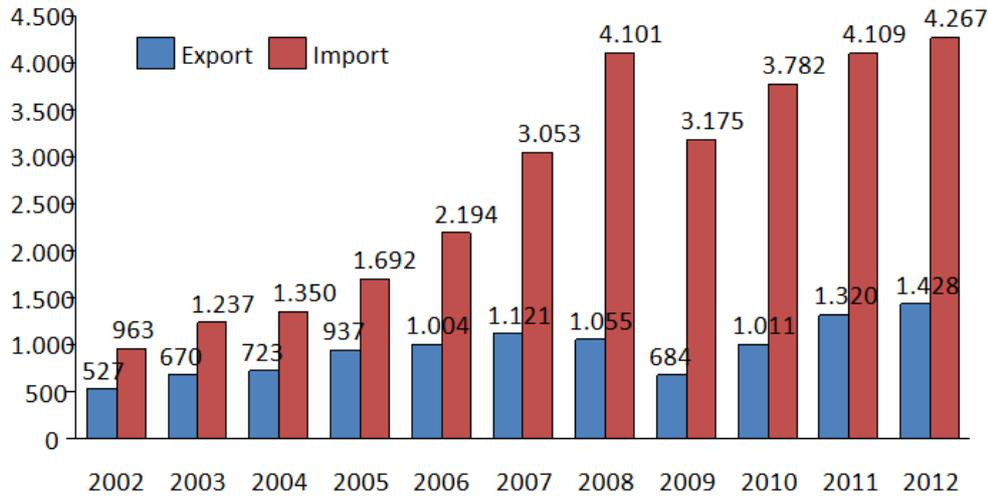
Sector Name	Exports, million USD
Edible fruit and nuts; peels of citrus fruit or melons	170
Iron and steel	110
Tanning or dyeing extracts; tannins and their derivatives; dyes	45
Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	36,3
Albuminoidal substances; modified starches; glues; enzymes	33,9
Plastics and articles thereof	29,7
Meat and edible meat offal	27,4
Salt; sulphur; earths and stone; plastering materials, lime and cement	26,2
Furniture; bedding, mattresses, mattress supports, cushions and similar	24,2
Oil seeds and oleaginous fruits; miscellaneous grains, seeds and fruit	20,3
TOTAL	746

Source: TUIK, TEPAV Calculations.

Armenia

In the last ten years, Armenia's trade deficit increased seven-fold in terms of volume. Armenia's imports have increased rapidly peaking at USD 4.2 billion in 2012, and while exports have increased at a slower pace than imports, export volume tripled since 2002, reaching USD 1.4 billion in 2012.

Figure 11: Exports and Imports of Armenia, million USD



Source: Comtrade, TEPAV Calculations.

Armenia exports 1634 different types of products. It's main export partners are the Russian Federation, Germany, and Bulgaria—accounting for almost 40% of all of Armenian exports. Aside from Russia and Iran, which are close by, Armenia has a set of diverse export partners compared to Turkey's eastern regions, with European countries as well as the USA and Canada amongst its top export destinations. Hence, in 2012 Armenia's average export distance stood as high as 3719 km. Armenia is a major exporter of Oreslag and Ash, gold, beverages, spirits, and vinegar.

Table 12: Top Export and Import Partners of Armenia, 2012

Country Name	Exports, million USD	Country Name	Imports, million USD
Russia	277,8	Russia	1.052
Germany	153	China	397
Bulgaria	129,2	Iran	219,4
Belgium-Luxembourg	127,1	Ukraine	215,8
Iran	94,2	Turkey	213,1
USA	87,2	Areas, nes	189,6
Canada	85	Germany	169
Netherlands	79,7	Italy	166,4
Georgia	78	USA	129,8
Switzerland	71,3	Brazil	93

Source: TUIK, TEPAV Calculations.

Table 13: Armenia's Top Ten Export Sectors, 2012

Sector Name	Exports, million USD
Oreslag and ash	279
Beverages spirits and vinegar	187
Natural or cultured pearls; precious or semi-precious stones; precious metals	173
Iron and steel	119
Copper and articles thereof	111
Mineral fuels; mineral oils; and products of their distillation	108
Aluminium and articles thereof	88
Aircraft; spacecraft; and parts thereof	48,8
Tobacco and manufactured tobacco substitutes	41,9
Nuclear reactors; boilers; machinery; and mechanical appliances; parts thereof	24,3
TOTAL	1.428

Source: TUIK, TEPAV Calculations.

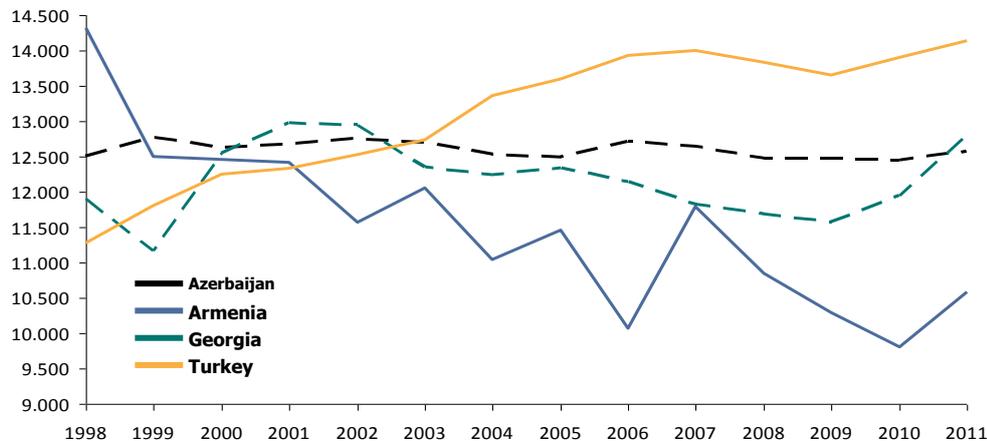
Quality of Exports

There is a strong correlation between export sophistication levels of a country and its GDP per capita. Export Sophistication (EXPY) developed by Hausmann, Hwang and Rodrik (2007) at Harvard University aims to capture the productivity level associated with a country's exports. EXPY is a proxy for the most productive set of products the country can produce at a given time, and can be computed for different categories of exports as well as for the entire export basket of a country¹⁷.

In 2011, Turkey's export sophistication value was the highest in the region, followed by Azerbaijan and Georgia, and then Armenia, which had the lowest EXPY value. The Turkish export sophistication index has increased steadily since 1998, except for a slight decrease during the 2008 crisis. The quality of Armenian exports reacted far more dramatically to the 2008 crisis, in 2010 dropping to their lowest point since 1998. In the past two years, the quality of Armenian exports has been rising at a faster rate than the quality of Turkey's exports.

¹⁷ To calculate the EXPY, first another indicator, PRODY, is calculated for each product as follows: *The weighted average of per capita GDP values where the weights represent the Revealed Comparative Advantage of each country in that product.* PRODY represents the productivity level associated with a product. The EXPY index is constructed for each country as a weighted average of the PRODY values of the products that the country exports. Hence, EXPY represents the productivity level associated with a country's export basket.

Figure 12: EXPY Evolution of Armenia and Turkey, 1998-2011



Sources: BACI Database, Penn World Tables 7.2, TEPAV calculations

TCl (Trade Complementarity Index)

The Trade Complementarity Index measures compatibility of trade profiles of countries. It also shows how well the structures of a country's imports and another country's exports match, revealing potential complementarities in addition to existing ones. The index value is equal to zero when one country's exports and another country's imports do not match, and to 100 when they match perfectly. We use the same methodology with the regional data to calculate the degree to which Turkey's regions complement Armenia's trading structure.

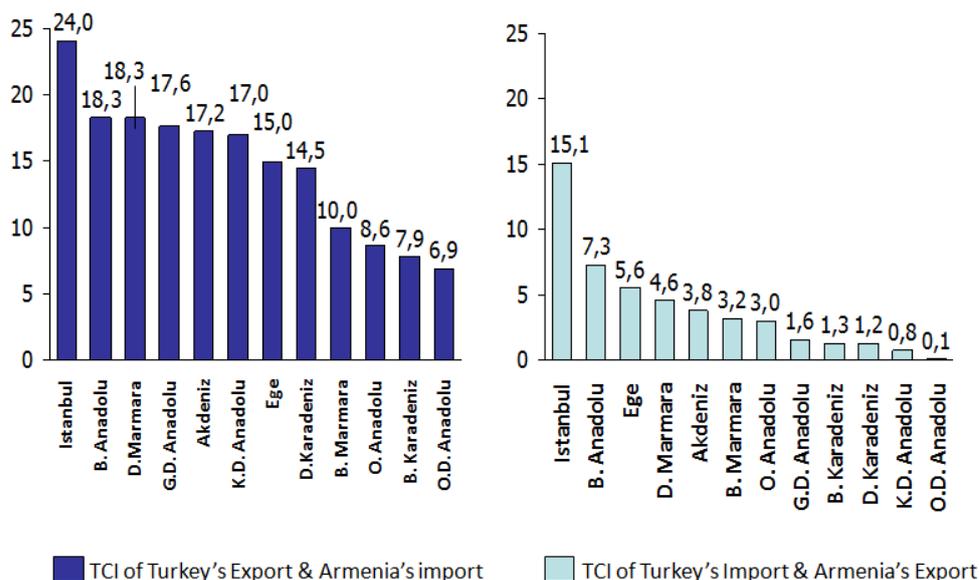
The results of the analysis do not show strong complementarity between Turkey's NUTS1 regions' exports and Armenia's imports. The average export complementarity of Turkey's regions with Armenia was only 14,6 in 2012.¹⁸ Instead, Armenia's trade profile was most compatible with the Istanbul region. This is largely due to the large range of products that are produced in the Istanbul region, which produces 95% of products in Turkey's production basket¹⁹. On the other hand, the eastern regions that have low complementarity with Armenia export only 16% of the commodity types that are produced in Turkey.

Looking at it the other way around, complementarity between Turkey's NUTS 1 regions' imports and Armenia's exports is also low. Again, the region that had highest import complementarity with Armenia's exports was Istanbul, albeit the complementarity value was still very low at 15% in 2012. This is largely due to the fact that Armenia's export bundle is not very diverse, exporting only 1864 different products in 2011.

¹⁸ TCI has been calculated with six-digit HS trade data which is taken from Turkish National Statistic Agency (TUIK). Due to firm level privacy of institution export volume between used data and public data on TUIK's website does not match. All the TCI calculations made with six-digit HS data, because of the difference some calculation mistakes may occur.

¹⁹ BACI database on six-digit classification contains 5023 different products.

Figure 13: Turkey's NUTS1 regions export & import complimentarity with Armenia, 2012



Sources: BACI, TUIK, Comtrade, TEPAV Calculations.

Similarly, the product-level analysis shows that Armenia's top import and exports do not match Turkey's NUTS1 regions' export and import baskets, respectively. Table 14 (See below) shows Armenia's top ten exports, export volumes for each product type, and the percentage change in export volume between 2002 and 2012. Turkey's import volume for each of the products Armenia exports is presented on the far right hand column, and signs on the far right side show whether Armenia's exports match the imports of Turkey/TRB/ TRA (matches are indicated by the colored-in circles). We can infer from the Table that Armenia's top export products do not have a large market in Turkey.

Table 14: Armenia's exports vs TRA, TRB and Turkey's imports, million USD, top 10 products

HS2	HS2 Name	Armenia's Export	2002-2012 Change	TRA TRB TR
26	Oreslag and ash	279	316,2%	● ● ●
22	Beverages spirits and vinegar	187	1343,9%	○ ○ ○
71	Natural or cultured pearls	173	889,1%	○ ○ ○
72	Iron and steel	119	702,7%	○ ○ ○
74	Copper and articles thereof	111	-33,2%	○ ● ●
27	Mineral fuels and oils, crude and distilled	108	930,1%	○ ○ ○
76	Aluminium and articles thereof	88	849,1%	● ● ●
88	Aircraft spacecraft and parts thereof	48.8	397,3%	○ ○ ○
24	Tobacco and man. tobacco substitutes	41.9	162,8%	○ ○ ○
84	Nuclear reactors, boilers, machinery	24.3	19783,6%	● ● ●

Sources: BACI, Comtrade, TEPAV Calculations, 2012

Similarly, Table 15 shows Armenia's top ten imports, import volumes for each product type, and the percentage change in import volume between 2002 and 2012. Turkey's export volume for each of the products Armenia imports is presented on the far right hand column, and signs on the far right side show whether Armenia's imports match the exports of Turkey/TRB/ TRA

(matches are indicated by the colored-in circles). We can infer from the table that there are complementary products available for enhancing Armenian imports coming from Turkey.

Table 15: Armenia's imports vs TRA, TRB and Turkey's exports, million USD, top 10 products

HS2	HS2 Name	Armenia's Import	2002-2012 Change	Turkey's Export	
27	Mineral fuels and oils, crude and distilled	902,9	434.99%	7,708	●●●
84	Machinery, boilers,	385,5	636.40%	11,999	○●●
85	Electrical television image and sound	212,8	337.86%	9,373	●●●
99	Complete industrial plant	186,5	941.58%	148,2	●●●
71	Natural or cultured pearls	178,7	-15.27%	16,325	○●○
87	Vehicles other than railway or tramway	169,4	617.09%	15,148	○●○
10	Cereals	152,5	211.75%	170,3	●●●
39	Plastics and articles thereof	119,9	650.26%	5,012	○●○
30	Pharmaceutical products	110,9	361.11%	661,7	○●○
72	iron and steel	102,4	593.62%	11,332	●●●

Sources: BACI, Comtrade, TEPAV Calculations, 2012

Concluding Remarks for the Product (micro-level) Assessment

Overall Trade Trends. Turkey has strong economic relations, with its neighbors while Armenia's economic interactions in the region are limited due its landlocked territory as well as the closure of two of its borders. Armenia has tried to overcome the negative effects of low cross-border trade by using air freight, as reflected in the high average export distance of Armenian products and in its large export volume compared to its neighbor regions, TRA and TRB, which are also geographically constrained.

Export Volume. Armenia's export volume tripled since 2002, while the TRA and TRB regions' exports increased six-fold since 2002. In 2012 Armenia's export volume (USD 1428 million) was about twice the size of the TRB region's export volume (USD 747 million), and about eight times more than TRA region's export volume (USD 181 million).

Trade Balance. In the last ten years, Armenia's trade deficit increased sevenfold. The TRA region generally ran a trade surplus since 2002, although the difference between the regions import and export volumes narrowed down significantly in 2012. In contrast, the TRB region's export volume stood at more than triple its import volume in 2012.

Export items. Armenia is a major exporter of Oreslag and Ash, gold, beverages, and spirits and vinegar, while the growth of TRA region's exports was driven by iron and steel. The TRB region's export surplus is driven by increase in the production of edible fruits and nuts and peels of citrus fruit or melons, as well as by iron and steel exports.

Product diversity. Out of the three regions the TRB region has the most diverse product basket—exporting 1864 types of products, compared to the 1634 types of products exported by Armenia, and the 804 product types exported by the TRA region.

Export distance. Armenia has a set of diverse export partners compared to Turkey's eastern regions with European countries as well as the USA and Canada amongst its top export destinations. The TRB region also exports goods to geographically far away countries such as

China and USA, while regional countries take the major share of the TRA region's exports. In 2012 the export distances for Armenia, the TRB, and the TRA were 3719 km , 2323 km, and 1577 km, respectively.

Quality of Exports. In 2011, Turkey's export sophistication value (EXPY) was the highest in the region, followed by Azerbaijan, Georgia, and Armenia. The Turkish export sophistication index has increased steadily since 1998, except for a slight decrease during the 2008 crisis, while the quality of Armenian exports reacted far more dramatically to the 2008 crisis.

TCI (Trade Complementarity Index). The results of the analysis do not show a strong complementarity between Turkey's TRA and TRB regions' exports and Armenia's imports. Instead, Armenia's trade profile was most compatible with the Istanbul region largely due to the large range of products that are produced in the Istanbul region. Looking at it the other way around, complementarity between Turkey's TRA and TRB regions' imports and Armenia's exports is also low. The Istanbul region had highest import complementarity with Armenia's exports albeit the complementarity value was still low due to the limited diversity of Armenia's export basket.

Product-level analysis of trade complementarity. The analysis also shows that Armenia's top imports and exports do not match Turkey's NUTS1 regions' export and import baskets, respectively. Armenia's top export products do not match imports of Turkey, the TRB region, or TRA region. We can infer that Armenia's main export products do not have a large market in Turkey. Conversely, Armenia's top imports products do not match exports of the TRB region or TRA region, while Turkey's exports are a better match for Armenia's top imports. We can infer that there are complementary products available for enhancing Armenian imports coming from Turkey.

The product micro-level assessment points to low level trade complementarity between Armenia and Eastern Turkey. However, the product level analysis does not include trade in services. Moreover, product analysis includes only past data and does not reflect recent economic activity or structural transformation. Yet, it is exactly such transformation—guided by the appropriate industrial policy—that can create future complementarities between the two countries. The next section will look closer at domestic sectoral developments with an aim to shed light on new opportunities for regional cooperation.

3.3 Sector (meso-level) Assessment

In this section we assess the main features of key sectors in Armenia and Turkey based on the comparative advantages of the two countries, and identify possible synergies (i.e. market access, skills complementarity) that can arise from economic interaction. The sectors that have been evaluated include construction, tourism, ICT, healthcare, agro-food, and textile and apparel sectors. Most of these sectors are services related where comparable quantitative data is limited. Stakeholder interviews collected during our fact-finding mission to Armenia—in addition to sectoral reports, national and regional strategy documents and reports prepared by other organization such as development agencies—formed an important part of the analysis for the services sectors.

Construction

The construction sector is an integral part of the Armenian economy, constituting 14% of GVA, and 4% of employment.²⁰ Starting in 2003, the government adopted a strategy aiming to attract investments from the Armenian Diaspora into the real estate sector, which resulted in a boom in the construction of residential units. Between 2003 and 2008, the value added of the sector increased more than five-fold, and the sector became an important component of GDP and employment growth.

However, the real estate- and construction-led economic growth led to an over-reliance on foreign exchange to finance high rates of investment, and the sectors were severely affected by the global financial crisis due to declines in remittances and investments. Between 2008 and 2012 the share of the construction sector in GDP shrank from 28% to 12%.²¹ Recently, the sector has taken a positive turn, growing 3.3% in 2012 partly due to the construction of the North-South highway. According to a recent World Bank report (2013), the sector is expected to grow between 3 and 4% annually in the future.²²

The World Bank's positive projection notwithstanding, opinions regarding the future growth prospects of the Armenian construction and real estate businesses continue to be divided. While some claim there is already an oversupply that needs to be absorbed, others see the sector as re-emerging. The findings of this research show the sector has long-term growth prospects in multiple areas, including rising demand for residences, hotels, and shopping malls, as well as large-scale infrastructure projects and the real estate management market. One argument is that demand for residential estates will continue to grow. Armenians tend to put their savings into real estate, as home-ownership is considered an important social and financial asset, especially for Armenians who live outside of Yerevan. The recent deregulation of rules governing foreign ownership of residences also boosted real estate demand from abroad.

Furthermore, Yerevan is the center of the manufacturing industry, which raises the real estate prices of the capital region. The price for a square meter of industrial land in Yerevan's suburbs is expensive—costing USD 80 on average²³. Office spaces in Yerevan are also expensive (price per square meter ranging from USD 3,000 to USD 10,000). In effect, the high cost of real estate makes the construction sector attractive for investors.

²⁰ CEIC database

²¹ World Bank 2013a

²² Ibid.

²³ Average price for a square meter of industrial land in Turkey's underdeveloped regions starts from USD 10 in middle-income emerging regions, i.e., Konya; prices range between USD 40 and USD 100; and in Istanbul as high as USD 500.

Lastly, the Armenian government's new industrial policy strategy that emphasizes development of the manufacturing sector is consistent with the emphasis on large-scale investments (See Section on *Policy Framework and Institutional Assessment*). For instance, the construction of the North-South Corridor in 2012 suggests that building infrastructure will be an important area for investment in the future.

Moreover, although constrained by its small size, real estate management is a dynamic market for investors. Large-scale projects such as construction of industrial buildings and zones can ensure that both the construction sector and real estate management market continue to grow. Managing real estate, especially hotels, shopping malls, and industrial zones, constitutes further opportunities along the value chain.

Opportunities for the Turkish Private Sector

Construction of infrastructure, hotels, and shopping malls, as well as the real estate management market, provide opportunities for Turkish businesses. Turkey is already an important supplier of building materials to Armenia's construction sector. In 2012, wood and wood articles constituted Turkey's second most important export items to Armenia (USD 18 million), while steel and steel articles came in tenth place (USD 10 million). This is largely due to the high logistical costs associated with construction materials such as cement, iron, and steel. It is more cost-effective to produce these locally.

The high costs associated with trading heavy materials notwithstanding, the construction value chain offers other possibilities for cooperation. For instance, Turkish companies were involved in the construction of the Zvartnots airport as subcontractors.

However foreign investors face numerous challenges in Armenia. Excessive regulation in the Armenian construction market and local orientation of the sector require that foreign businesses work with local partners in order to deal with complicated construction permits and licenses, find suppliers, and reach customers. Therefore, it is important to develop interaction platforms and mechanisms for Turkish businesses interested in entering the Armenian construction market to meet their local counterparts.

Tourism

The Armenian tourism sector has been growing rapidly at an average annual rate of 23%. The sector was relatively unaffected by the economic crisis generating a revenue of USD 485 million from 748,000 international visitors in 2011²⁴. However, the Armenian tourism sector does not live up to its full potential, with hotels and restaurants continuing to account for only about 1% of the economy and employment²⁵. The most important challenge facing the Armenian tourism sector is the lack of connectivity in the region. Moscow and Tehran are the only cities that have direct flights to Yerevan's Zvartnots Airport on a daily basis. The closure of borders restricts most transportation possibilities to air travel, which is expensive and limited. The lack of an effective marketing strategy exasperates low demand and keeps travel costs high.

There are three types of tourism in Armenia: cultural, winter, and health. The most dominant type is cultural tourism. Armenia attracts visitors from Europe and the Armenian Diaspora to destinations such as Ecmiadzin and the Garni Temple. An important portion of tourists visit

²⁴ World Bank Development Indicators

²⁵ CEIC Database

Armenia as a part of South Caucasus tours, spending about one week in the country. Armenia also attracts large numbers of Iranian tourists for New Year's Eve and Nawroz.

The main destination for winter tourism is Tsakhkadzor, which attracts a small number of tourists (mostly from Russia) between December and March. The infrastructure, which was initially built to prepare Soviet athletes for the 1988 Winter Olympic Games, underwent significant renovation in 2008. Nevertheless, the number of visitors remains low due to expensive flights and hotels.

Lastly, health tourism attracts the Armenian communities abroad who prefer to come to Armenia for treatment (particularly for dental surgeries) because of significantly lower costs compared to Europe or North America. Moreover, Armenia's healthcare system offers quality healthcare providers and qualified healthcare professionals. The high quality of physicians in Armenia can be partly explained by Soviet-era institutions as well as Armenians who were educated in Moscow and more recently in the US.

Opportunities for Turkish-Armenian Cooperation in the Tourism Sector

Cultural similarities between Armenia and Turkey, reflected in the traditions and cuisine, provide opportunities for cooperation. Turkey is already among Armenian tourists' top holiday destinations. According to the Turkish Ministry of Tourism and Culture, 70,000 Armenians visited Turkey in 2012.²⁶ Antalya, which has direct charter flights to Yerevan, is a popular destination for summer holidays. Other popular destinations include Istanbul, Van, Adana, Mersin, Elazığ, and Cappadocia. Tours usually last between 3 and 11 days and use buses to travel through Georgia.

On the other hand, only about 1000 visitors from Turkey visit Armenia each month including truck drivers. The closure of the Turkish-Armenian border, for instance, has had a negative effect on tourism. Moreover, long travel times reduce the popularity of tours between Armenia and Eastern Anatolia. Travel times from Yerevan to Van last as long as 22 hours. There has been an initiative to introduce flights between Van and Yerevan, which would reduce travel time between the two cities to less than one hour. However, the planned flights were cancelled in early 2013, in spite of the high level of interest. Scheduled flights between Van and Yerevan could have made Eastern Anatolia part of the South Caucasus tours.

Increased connectivity in general would bring tourists as well as business people from Eastern Anatolia to Yerevan, which is the largest city in the region, with a dynamic economic and cultural life. Armenia also has the potential to become a tourism destination for Turkey's growing middle class. One way to overcome transportation constraints is to organize luxury tour packages for wealthy clients or to promote medical tourism by introducing special licenses that permit helicopters to travel between Yerevan and Eastern Turkey.

An important step towards increasing tourism is to increase the frequency of direct flights between Istanbul and Yerevan. The government recently deregulated the civilian air transport industry and the national flag carrier, Armavia, went bankrupt in April 2013. The government's *Open Skies* policy will make the Armenian aviation market more competitive and is expected to increase flight frequency, bring down prices by 10%, and increase tourism revenues by 20-25% (See section *The "Open Skies" Policy*). However, the recent deregulation has not affected flights between Istanbul and Yerevan, as these are charter flights. The charter flights fly only

²⁶ Ministry of Tourism and Culture of Turkey Statistics

twice a week and are expensive. A comparison with the Istanbul-Tbilisi route reveals the high cost of the Istanbul-Yerevan flight: the Istanbul-Tbilisi round-trip flight was about USD 220, compared to USD 550 for Istanbul-Yerevan round-trip with Armavia airlines²⁷.

Lastly, tourism alliances can be formed between the Turkish and Armenian private sectors. The Armenian tourism agencies interviewed in Yerevan noted that Turkey has better human resources, training, and more experience in the tourism sector. Therefore, promoting partnerships between Turkish and Armenian tourism agencies and encouraging sectoral stakeholders to work together (i.e. exchange programmes for tourist guides) can help Armenia to capitalize on Turkey's knowledge in the sector.

Information and Communications Technology (ICT)

The ICT sector is one of the most dynamic and promising sectors of the Armenian economy. The ICT potential of Armenia was built on the strong math and science foundation established during the Soviet era. Moreover, Soviet Armenia was a center for high-value manufacturing for the USSR. The collapse of the Soviet Union was followed an influx of large US companies such as Boomerang Software (internet applications), Credence Systems (semiconductor design-to-test solutions), Cylink (network security products and VPN solutions), Epygi Technologies (IP PBXs), HPL Technologies (yield management software and test chip solutions), Virage Logic (advanced embedded memory IP), and others²⁸ that sought to take advantage of Armenia's qualified workforce. The new entrants to the market created new opportunities for the industry, which gradually shifted from manufacturing to software and services related areas.

More recently the Armenian government declared IT & Telecom sectors as key priority areas that can generate well-paying jobs for the youth²⁹. An ICT leader in its region, Armenia already has a high number of graduates in the ICT field and offers competitive labor costs.

Armenia's ICT sector comprises of three main areas: IT, telecom, and engineering. The combination of all three areas performs at a higher level compared to other growing sectors such as construction, tourism, retail, and agro-food. Compound annual growth rate (CAGR) of the ICT sector between 2008 and 2011 was around 22%, whereas average annual growth rates (AAGR) of agriculture and food processing were only 10.4% and 11.3%, respectively³⁰. ICT is also one of the top export-sectors, as economic activity in this sector is not affected by physical constraints such as Armenia's closed borders. In 2010 the sector accounted for 8.5% of exports and the CAGR of ICT exports was 8.9% during the period between 2008 and 2011³¹. The ICT sector is also an important source of employment. Between 2008 and 2010, the sector created around 5,000 new jobs, 83% of which are technical specialists and the remaining 17% were business & management specialists.³² Furthermore, the IT, telecom, and engineering sectors combined contribute above 6% to Armenia's GDP, while the ICT sector's

²⁷ The cost is for December 2013 flights. Turkish Airlines and Pegasus Airlines fly between Istanbul and Tbilisi, for which the cost was 166 € and 152 €, respectively.

²⁸ Enterprise Incubator Foundation 2009

²⁹ EV Consulting 2012

³⁰ *ibid.*

³¹ EV Consulting 2012, World Bank 2013a

³² World Bank 2013a

contribution to national GDP in India or the US is about 3%.³³ Although the ICT sector is relatively mature, there is room for significant expansion in the market.

The IT sector is the most dynamic among the three subsectors, with at least 300 companies that specialize in Internet services, web development, and IT consulting³⁴. Major national and international players in the IT sector include Synopsis, Microsoft, Credence Systems, Mentor Graphics, Armsoft, Instigate, and Cambric Armenia. While historically, large companies dominated the Armenian IT market, the revenue shares of these have been decreasing and SMEs have increased in importance in the last five years. Since 2007, the number of small firms with revenues less than USD 100,000 increased by 19%, and their share in total industry revenues grew by 3%³⁵.

The fully-liberalized telecom subsector's industry output was much higher compared to the IT sector, while its CAGR was much slower (4.6% between 2006 and 2011), which reflects the relative maturity of the telecom industry. The sector employs only 0.7% of the workforce (8,500 persons). Almost all players in the telecom sector are foreign companies (predominantly Russian), providing services such as mobile & fixed telephony, cable & wireless Internet, the provision of IT infrastructure, and VoIP services. For instance, 46% of Internet Service Providers (ISPs) are foreign-owned companies; the five largest ISPs, only one of which is a domestic company, account for 83% of the Internet services revenue.³⁶

One of the major challenges facing the sector is the shortage of qualified professionals. According to the World Bank, employability of higher education graduates in the sector is very low. It is pivotal to increase the attractiveness of the ICT sector for young higher education graduates and provide them professional training for the continued dynamism of the sector. Secondly, the industry suffers from an absence of high-quality transport infrastructure and competitive facilities, such as office space. Lastly, the regulatory environment lacks transparency, stability, and predictability, with implications on intellectual property and data protection rights.

Opportunities for Turkish-Armenian Cooperation in the ICT Sector

The effective coordination of the complementary assets of Turkish and Armenian SMEs can result in mutual gains. Strategic interactions between SMEs based on their comparative advantages are also the most effective way to promote long-lasting links in the region and achieve an equal distribution of the benefits of growth. While Armenia has a qualified and relatively cheap labor force, Turkish SMEs can offer competitive facilities and infrastructure, e.g., office space and equipment. Turkey's young, urban population is also an attractive market for Armenian firms.

Second, cooperation between Turkey and Armenia can promote entrepreneurship at the regional level. The combination of Turkey's entrepreneurial environment—which has a relatively well-developed network of angel investors, accelerators and mentors—and Armenia's pool of

³³ EV Consulting 2012, World Bank 2013a

³⁴ World Bank 2013a

³⁵ Enterprise Incubator Foundation 2013.

³⁶ ISP Armenia's ISPs offer ADSL, fiber-optic and cable access, WiFi-WiMax wireless, GPRS, EDGE, CDMA and 3G technologies. The services except fiber-optic network are offered throughout most of the country. One of the crucial developments was the introduction of 4G/LTE network by VivaCell-MTS in 2011.

potential entrepreneurs, could build an entrepreneurship ecosystem in the region. Turkish entrepreneurs can also utilize Armenia's human capital in the ICT sector in order to enter the Russian and CIS markets.

Healthcare

The main advantages of the Armenian healthcare sector include quality physicians, competitive oncology facilities, and strong connections to Europe and the US through the Armenian Diaspora. On the other hand, lack of access to affordable primary healthcare poses a serious challenge to Armenia's healthcare system. In order to tackle low healthcare access, the Government of Armenia introduced a mandatory health insurance scheme for employees working at different state organizations and civil servants. However, private spending continues to account for a large share of healthcare expenditures.

Armenia's healthcare sector is at a developmental stage. Government health care expenditures gradually increased in the past decade with an average annual growth rate of 16% during 2002-2011³⁷. However, the share of public expenditures in healthcare is still very low at 1.5%. Public expenditures are aimed towards improving the quality of medical centers, developing nuclear medicine, promoting the pharmaceutical sector, and increasing the quality of primary healthcare.

As a result of large number of mergers of various medical institutions through structural optimization of the industry, the key players in the healthcare sector are private large hospitals with multifunctional facilities. Today, the market structure of the sector is a monopolistic competition dominated by ten major companies. The healthcare sector's gross value added reached almost USD 400 million, with an average annual growth rate of 15.6% during 2007-2011, employing 3.6% of the total workforce in 2010.

Armenia's technical advantages are in the areas of heart surgery, therapy, dental, and plastic surgery as a result of its acclaimed local hospitals and doctors³⁸. One of the highlights in the healthcare sector is the increasing exports of some health services. Local hospitals and individual physicians receive widespread acclaim, especially in areas such as cardio and plastic surgeries, eye treatment, and dental services. The Armenian Diaspora constitutes the main customer base for medical operations. The dental surgery industry, in particular, has rapidly expanded after gaining international recognition for its delivery of high quality, low-cost care.

Another emerging area of healthcare is the nuclear medicine sector, where Armenia has the potential to become a regional center for the diagnosis and treatment of oncological and cardiovascular diseases. Recently, the National Competitiveness Foundation of Armenia (NCFA) established the ambitious Armenian Center of Excellence in Oncology (ACEO). The center will include a diagnostic center with PET scanners, a laboratory, and an oncology clinic. A total amount of EUR 20 million was invested in the project and the NCFA will utilize the Armenian Diaspora for the operations and management of ACEO. One board member of the NCFA is Haig Bagerdjian, who is also the CEO of Global Medical Solution—a leading-edge provider of nuclear medicine and diagnostic imaging products & services across Asia & Australia.³⁹

³⁷ EV Consulting 2012

³⁸ *ibid.*

³⁹ Global Medical Solutions Website

Lastly, the pharmaceutical industry is more developed than the medical services sectors. The industry is dynamic and competitive, with 17 licensed local generic drug producers, 30 importing companies, 20 distribution companies, and 1,500 pharmacies. The sector is also highly export-oriented, with 65% of domestic production being exported to CIS countries and Georgia in 2012.⁴⁰

Opportunities for Turkish-Armenian Cooperation

Armenia and Turkey can cooperate on multiple fronts in the healthcare context. In order to address low level of access to healthcare in Armenia, Turkish firms can invest in the building of cost-effective healthcare facilities. In turn, Turkish citizens living in the Eastern Anatolian region with limited access to healthcare facilities can take advantage of Armenia's high quality health care at a lower cost than is available in Turkey's Istanbul region.

Agriculture - Food and Beverages

Agriculture and food processing are key economic activities in Armenia, accounting for approximately 30% of GDP, and contributing significantly to Armenia's trade. Armenia is a net importer of food products: imports were five times higher in volume than exports. Imported food products also serve as inputs in the production of key goods such as wheat. As a result of import quantity, price levels in Armenia are higher compared to other countries, after adjusting for GDP per capita (i.e. about 17% higher on average than CIS countries), although price differences vary from product to product.⁴¹

The high volume of food imports notwithstanding, agriculture and food processing are dynamic production sectors. Despite continuous fluctuations, the agriculture sector continued to grow in the post-crisis period at an average rate of 10.4% between 2007 and 2011.⁴² The agricultural sector accounted for 22.2% of national GDP and 39% of the workforce (457,400 people) in 2011. Agricultural exports reached USD 314 million in 2012.

The share of GDP contribution was lower in food processing (8.5% in 2012) than in agriculture; the value of food processing exports at USD 183.8 million was also much lower. On the other hand, the sector grew at a rate of 11.3% between 2007 and 2011, slightly higher than growth rate of the agriculture sector. The growth in exports and imports were almost the same.

The two main sub-sectors of food processing are alcohol and canned-food production. Dairy products are also produced, but primarily for the domestic market. The export-oriented canned food industry is comprised of establishments primarily engaged in preserving vegetables and fruits. The industry is split between four to five large producers which target Armenian communities abroad. Similarly, large-scale investors dominate the beverage sub-sector.

The largest beverage producer in the country is Yerevan Brandy Company, which has produced cognac since 1887. Armenia is the sixth-largest exporter of Brandy in the world and 90% of their production is exported to Russia. More recently, China and other Asian countries have become important export markets. The French beverage conglomerate Pernod Ricard bought the Yerevan Brandy Company in 1999.

⁴⁰ EV Consulting 2012

⁴¹ World Bank, Armenia Country Economic Memorandum 2013

⁴² Average Annual Growth Rate (AAGR)

On the other hand, the wine industry is split between many small producers, although there are exceptions. For instance, "Tierras de Armenia", owned by Eduardo Eurnekian, a Latin American business tycoon and member of the Armenian Diaspora, invested USD 40 million in land and a winery in the Armavir region to produce high quality wines. Similarly, Spayka Group invested in the establishment of a modern refrigeration complex that cost an estimate of USD 45 million. The agriculture and food processing sectors in Armenia present opportunities for investors. Armenia's high-quality land provides excellent conditions for high-volume production, and the country is relatively investor-friendly, offering favorable tax and customs regimes. Labor is abundant and cheap, although the workforce suffers from low skill levels. Moreover, outdated production methods and a lack of established and effective production supply chains pose serious challenges to investors.

Textiles and Apparel

The textiles and apparel sector is one of the oldest industries in Armenia, which was a major supplier of garments and textiles to the Soviet Union. The sector accounted for over one-quarter of the total workforce during the Soviet Era, employing 115,000 people (or 25-30% of the country's labor force) during the 1980s. Today, the textiles industry continues to employ more than a quarter of the workforce.

In 2011, the Armenian government listed the textiles and apparel industry among 11 strategic export-oriented sectors in its new industrial strategy. Export of textile and textile articles reached USD 55 million, or 8% of total exports in 2012.⁴³ Similarly, the share of textile and textile articles imports, of total imports, was 8.5%, although imports were less than half, in volume (USD 23 million in 2012), than exports.

Armenia's biggest export partners in textiles are CIS countries, with which Armenia enjoys free trade privileges. More recently, Armenia's export markets expanded to include Europe and America. Large producers that mainly specialized in clothing, knitting, and textile processing dominate the Armenian textile and apparel industry, although the number of firms, as well as employment in the sector, has been increasing after the crisis.

Improvements notwithstanding, production is far less than what is optimal, as the sector faces numerous challenges. Production depends on imported raw materials and producers face high transportation costs. As a result there are only a few local brands. On the other hand, lower labor costs makes Armenia an attractive destination for foreign investors (the average monthly wage for textile workers is approximately USD 200). Larger FDI flows into the sector could foster technological upgrading, increase productivity, and improve marketing and sales practices. The transformation of the sector is all the more urgent given that some of the largest producers still work below average capacity. In order to attract investors to the sector, the Armenian government offers VAT exemptions for 3 years for the import of modern equipment for investments that are above EUR 585,000.⁴⁴

Opportunities for Turkish-Armenian Cooperation

Turkey is one of the biggest textile exporters in the world. According to WTO data, Turkey is the world's eighth-biggest textile exporter and fifth-biggest garment exporter. Moreover, the Turkish textile and garment industry, which enjoys a skilled-workforce and uses modern equipment

⁴³ World Trade Organizations (WTO) database

⁴⁴ East Invest 2011

and technologies, produces very high-quality exports, of which 70% compete in export markets targeted by China and other Asian countries. The main export partners of Turkey are European countries, the United States, and Russia.

On the other hand, Turkey does not have an important presence in CIS countries, while Turkey's presence in Russia's textile and garment imports is negligible—in spite of Russia being one of Turkey's main export destinations. Turkish textile producers that invest in Armenia could export goods to CIS countries (including Russia) tariff-free under the CIS Free Trade Agreement (or CISFTA, signed in 2011). Moreover, Turkish firms that invest in Armenia could improve their competitiveness by taking advantage of Armenia's low labor costs and under-utilized textile machinery.

Concluding Remarks for Sector (meso-level) Assessment

Construction. In 2003 the Armenian government adopted a policy strategy aiming to attract investments from the Armenian Diaspora into the real estate sector, which resulted in a boom in the construction of residential units. However, the real estate and construction sectors were severely affected by the global financial crisis due to declines in remittances and investments, although the sector took a positive turn in 2012 (partly due to the construction of the North-South highway). The findings of this research suggest that the sector has long-term growth prospects in multiple areas, including rising demand for residences, hotels, and shopping malls, as well as large-scale infrastructure projects and the real estate management market. While the sector provides opportunities for Turkish businesses, foreign investors face numerous challenges in Armenia, including excessive regulation and the local orientation of the sector that requires foreign businesses to work with local partners. Therefore, it is important to develop interaction platforms and mechanisms for Turkish businesses interested in entering the Armenian construction market to meet their local counterparts.

Tourism. The Armenian tourism sector has been growing rapidly at an average annual rate of 23%. However, the Armenian tourism sector does not live-up to its full potential, with hotels and restaurants continue to account for about 1% of the economy and employment. The most important challenge facing the Armenian tourism sector is a lack of connectivity in the region and the closure of borders, which restricts transportation possibilities to air travel, which is expensive and limited. The Armenian government's recent *Open Skies* policy deregulating the civilian air transport industry is an important step towards making the Armenian aviation market (served only by a single monopoly carrier until recently) more competitive, and is expected to increase flight frequency, bring down prices, and increase tourism revenues.

Increased connectivity would bring tourists as well as business people from Eastern Anatolia to Yerevan, which is the largest city in the region, with a dynamic economic and cultural life. Scheduled flights between Van and Yerevan would make Eastern Anatolia part of South Caucasus tours. At present, travel times from Yerevan to Van through Georgia last as long as 22 hours. Another way to overcome transportation constraints is to organize luxury tour packages for wealthy clients or to promote medical tourism by introducing special licenses that permit helicopters to travel between Yerevan and Eastern Turkey. Increasing the number of direct flights between Istanbul and Yerevan would also increase tourism. Moreover, tourism alliances can be formed between Turkey and Armenia. Promoting partnerships between Turkish and Armenian tourism agencies, and encouraging sectoral stakeholders to work together (i.e. exchange programmes for tourist guides), can help Armenia to capitalize on Turkey's knowledge in the sector.

Information and Communications Technology (ICT). The ICT sector is one of the most dynamic and promising sectors of the Armenian economy built on the strong math and science foundation established during the Soviet era. An ICT leader in its region, Armenia already has a high number of graduates in the ICT field and offers competitive labor costs. The Armenian government declared the IT & Telecom sectors as key priority areas that can generate well-paying jobs for the youth. Armenia's ICT sector is comprised of three main areas: IT, telecom, and engineering. The combination of all three areas performs at a higher level compared to other growing sectors, such as construction, tourism, retail, and agro-food. ICT is also one of the top export-sectors as economic activity in this sector is not affected by physical constraints, such as Armenia's closed borders. While the fully-liberalized telecom subsector's industry output is still much higher compared to the IT sector, the latter is more dynamic and includes major national and international players. While historically large companies dominated the Armenian IT market, the revenue share of these has been decreasing and SMEs have increased in importance in the last five years. The major challenges facing the sector include the low employability of higher education graduates, absence of high-quality transport infrastructure and competitive facilities (such as office space), and lack of transparency, stability, and predictability in the regulatory environment, with implications on intellectual property and data protection rights.

The results of the study show that effective coordination of complementary assets of Turkish and Armenian SMEs can result in mutual gains. First, while Armenia has a qualified and relatively cheap labor force, Turkish SMEs can offer competitive facilities and infrastructure, e.g., office space and equipment. Turkey's young, urban population is also an attractive market for Armenian firms. Second, cooperation between Turkey and Armenia can promote entrepreneurship at the regional level. The combination of Turkey's entrepreneurial environment—which has a relatively well-developed network of angel investors, accelerators, and mentors—and Armenia's pool of potential entrepreneurs, could build an entrepreneurship ecosystem in the region. Turkish entrepreneurs can also utilize Armenia's human capital in the ICT sector in order to enter the Russian and CIS markets.

Healthcare. Armenia's healthcare sector is at a developmental stage. In addition to the technical advantages in the areas of heart surgery, therapy, dental, and plastic surgery, the main advantages of the Armenian healthcare sector include quality physicians, strong connections to Europe and the US through the Armenian Diaspora, and the export-oriented pharmaceutical industry linked to CIS countries. The dental surgery industry, in particular, has rapidly expanded after gaining international recognition for its delivery of high quality, low-cost care. Another emerging area of healthcare is the nuclear medicine sector, where Armenia has the potential to become a regional center for diagnosis and treatment of oncological and cardiovascular diseases.

On the other hand, lack of access to affordable primary healthcare poses a serious challenge to Armenia's healthcare system. In order to tackle low healthcare access, the Government of Armenia introduced a mandatory health insurance scheme for employees working at different state organizations and civil servants. However, private spending continues to account for a large share of healthcare expenditures.

In order to address the low level of access to healthcare in Armenia, Turkish firms can invest in the building of cost-effective healthcare facilities. In turn, Turkish citizens living in the Eastern Anatolian region with limited access to healthcare facilities can take advantage of Armenia's high quality health care at a lower cost than is available in Turkey's Istanbul region.

Agriculture - Food and Beverages. Agriculture and food processing are key economic activities in Armenia, accounting for approximately 30% of GDP, and contributing significantly to Armenia's trade. The agricultural sector is mostly split between a large number of micro and small farms and enterprises. On the other hand, the food processing sector, including alcohol and canned food production, is split between large producers. The largest food processing company in the country is Yerevan Brandy Company.

The agriculture and food processing sectors in Armenia present opportunities for investors. Armenia's high quality land provides excellent conditions for high volume production, and the country is relatively investor-friendly through the offer of favorable tax and customs regimes. Labor is abundant and cheap, although the workforce suffers from low skill levels. Moreover, outdated production methods and lack of established and effective production supply chains pose serious challenges to investors.

Textiles and Apparel. The textiles and apparel sector is an important export sector, employing more than a quarter of the workforce. Armenia's biggest export partners in textiles are CIS countries, with which Armenia enjoys free trade privileges. More recently, Armenia's export markets expanded to include Europe and America. Large producers that are mainly specialized in clothing, knitting, and textile processing dominate the Armenian textile and apparel industry, although the number of firms as well as employment in the sector has been increasing after the 2008 crisis. Improvements notwithstanding, the sector faces numerous challenges, including dependence on imported raw materials and high transportation costs. On the other hand, lower labor costs makes Armenia an attractive destination for foreign investors. Larger FDI flows into the sector could foster technological upgrading, increase productivity, and improve marketing and sales practices. The transformation of the sector is all the more urgent given that some of the largest producers still work below average capacity.

Turkey is one of the biggest textile exporters in the world. The Turkish textile and garment industry, which enjoys a skilled workforce and uses modern equipment and technologies, produces very high quality exports. The main export partners of Turkey are European countries, the United States, and Russia. On the other hand, Turkey does not have an important presence in CIS countries, while Turkey's presence in Russia's textile and garment imports is negligible in spite of Russia being one of Turkey's main export destinations. Turkish textile producers that invest in Armenia could export goods to CIS countries (including Russia) tariff-free under the CIS Free Trade Agreement (or CISFTA, signed in 2011). Moreover, Turkish firms that invest in Armenia could improve their competitiveness by taking advantage of Armenia's low labor costs and under-utilized textile machinery.

In the *Sector (meso-level) Assessment* we evaluated a list of sectors including construction, tourism, ICT, healthcare, agro-food, and textile and apparel sectors, and identified possible synergies (i.e. market access, skills complementarity) between Armenia and Turkey that can arise from further economic interaction. The next section, *Policy Framework and Institutional Assessment*, provides a contextual setting (economic policies, policy environment and institutional structure) to accurately assess the political feasibility of economic cooperation in the region by identifying risks and opportunities presented under the current and future policy frameworks of Armenia and Turkey. The key findings of the sectoral and policy framework assessments will then be synthesized to identify sectoral areas (from the preliminary list) with the highest potential for synergies between the two countries.

3.4 Policy Framework and Institutional Assessment

This section assesses economic policies, policy environments, and institutional structures of South Caucasus countries, with a focus on Armenia. Most of the insights presented in this section were gathered during the fact-finding mission to Yerevan in November 2013. The main goal of the Policy Framework and Institutional Assessment is to establish a set of sectoral priorities by identifying risks and opportunities presented under the current and future policy frameworks of the Armenian and Turkish governments. The analysis is essential for placing the recommendations of this project in an accurate context, to complement the quantitative analysis, and to capture what is beyond existing datasets.

The section consists of a *Policy priority mapping* of flagship government policies, main public sector initiatives, and projects affecting private sector development and competitiveness. We gathered information from relevant strategy documents and interviews with stakeholders from development agencies and local chambers. The main political strategies discussed include Armenia's Export-Led Industrial Policy, the National Competiveness Foundation of Armenia (NCFA), EurAsEc Customs Union membership, and *Open Skies* policy, and Turkey's latest Five-Year Development Plan. As significantly, regional development policies of Turkey's eastern parts were evaluated. The analysis complements the other three (largely quantitative) assessment sections by providing a contextual setting to accurately assess the feasibility of regional economic cooperation in sectors and other areas discussed in the study.

Search for a new growth model in Armenia

In 2011, the Government of Armenia announced its new economic development strategy, the "*Strategy of Export-Led Industrial Policy*." The document published by the Ministry of Economy is a roadmap describing medium- and long-term measures to develop existing export sectors and those with export potential.⁴⁵ The plan aims to achieve transformation in targeted sectors by improving the business environment, lifting trade barriers, improving the infrastructure, and attracting foreign investment. The new economic policy is mainly focused on the manufacturing industry, which will be the main driver of export growth for the following decade. The eight sectors that have been indicated as ones with significant export potential—and that will be supported under the new economic policy—include metal mining, metallurgy, food production, gem and jewelry making, machine-building, instrument-making, electrical and technical production, chemicals, light manufacturing (textiles), and construction materials. In addition to tradable sectors, a number of services sectors were identified as priority areas to support industrial development: information and communication technologies, tourism, healthcare (including life sciences), education, and agriculture.

The key industrial strategy of the plan is to focus on high value-added, niche areas. Armenia is a small, geographically- and logistically-constrained country. Therefore, the most feasible strategy for manufacturing firms is to rely on foreign markets and to develop expertise in a small number of niche areas as well as utilize air transportation to export high value products. In this aspect, the development strategy of Armenia is comparable to that of Israel, which went from a closed and state-dominated economy in 1979, to a globally-competitive, high-tech giant. However, the success of Armenia's aim to become a high-value export economy depends on the effective implementation of its new development strategy.

⁴⁵ Republic of Armenia Minister of Economy 2011

The new plan also emphasizes the removal of trade barriers, and underlines the benefits expected from the Deep and Comprehensive Free Trade Agreement (DCFTA) with the EU. The DCFTA includes key reforms in areas—such as standardization, intellectual property rights, competition, and public procurement—that will help attract European investors and boost Armenia’s trade with the EU. The Agreement is also expected to enable Armenia to access the Turkish market more freely, while a separate treaty will be required to ease the movement of Turkish goods to enter the Armenian market.⁴⁶ Noteworthy, however, is the absence of a discussion of trade and cooperation with Turkey in Armenia’s export-based industrial strategy paper.

Furthermore, Iran is also expected to become a more important trade partner for Armenia, in spite of lack of connectivity in the region. The possible lifting of sanctions against Iran in the short- and medium-term, and the completion of the North-South Highway, are likely to expand trade between the two countries. The highway may also create opportunities for multinationals who wish to move their operations to Armenia and access the Iranian market.

Formal Links with the Armenian Diaspora

In addition to the new economic plan, the Government of Armenia founded the National Competiveness Foundation of Armenia (NCFA) in 2008, with the mission of creating formal links between the Armenian business community abroad and the Government of Armenia. The Foundation aims to build a knowledge-based economy by focusing on the healthcare, education and tourism sectors, and by transferring the capabilities and resources of the Diaspora community to serve national development. In coordination with funders from the Diaspora, the government aims to provide subsidized loans and equity financing as a source for ground financing. The Diaspora is also expected to help attract talent from abroad. A similar approach was successfully carried out in Chile, where the Fundacion Chile had a significant impact on transforming Chile’s fishing industry and education system. Likewise, the NCFA will focus both on private and public sectors though leveraging the financial capabilities and network of the Armenians living abroad.

Armenia’s EurAsEc Customs Union membership

In September 2013, Armenia announced its decision to join the Customs Union of Belarus, Kazakhstan, and Russia (EurAsEc). If Armenia becomes a full member of the EurAsEc this may negatively affect its trade relations with Turkey. Since the Customs Union has higher tariff rates on certain Turkish products than Armenia does, membership may impose additional costs on its trade with Turkey. It is therefore important to fully determine the exact impact of Armenian membership on different sectors. Armenia’s EurAsEc membership is unique in that the country is joining a customs union, which applies higher tariff rates than its own and may have large trade diversion effects on Armenian imports in general.

One way to tackle difficulties that may result from Armenia’s EurAsEc membership is to apply an internal processing regime, which grants tariff and tax exemptions to imports that will be used in the production of exports. The arrangement may help Armenia and Turkey jointly access third-party markets.

⁴⁶ Dizman 2013

The "Open Skies" Policy

The Armenia government is developing a strategic action plan to improve its air traffic. Most importantly, the government introduced an "open sky policy," which includes deregulation of the civilian air transport industry. According to the plan, all companies, regardless of nationality, will be able to operate flights after meeting a set of technical standards. Previously, market access of international carriers was subject to government approval. The bankruptcy of Armenia's national flag carrier Armavia, in April 2013, influenced the decision to adopt the *Open Skies* policy.

If the new policy is fully implemented, the Armenian aviation market will become more competitive. Ticket prices are expected to drop by 10% and the number of flight destinations and frequencies will increase⁴⁷. Increased connectivity is also expected to benefit the economy by increasing passenger and cargo volumes. The *Open Skies* policy is expected to contribute 1-1.5% per year to GDP growth create 20 thousand jobs and increase tourism revenues by 20-25%⁴⁸.

There are also international platforms that promote liberalizing market access as well as the compatibility and convergence of regulations. Turkey and Armenia are both members of the European Organisation for the Safety of Air Navigation (Eurocontrol) and European Civil Aviation Conference (ECAC), which seek to harmonize aviation practices. Both countries are also expected to join the European Common Aviation Area (ECAA) which aims to establish a single aviation market. If realized, this development will further ease the establishment of new flights between the two countries. The cancelled Van-Yerevan route may be resumed and new flight routes such as Bodrum-Yerevan may be introduced.

Priority Mapping

Armenia

Armenia's export-oriented, new industrial strategy document focuses on orienting the manufacturing industry towards high value products that will be shipped by air to global markets. The strategy aims to have long term positive impact on Armenia's export growth, which is constrained by its landlocked position. In order to achieve its aim, the government formulated a set of key objectives to be carried out during 2011-2020. The main objectives include development of the business environment, increasing the level of cluster development, and the sophistication of company strategies and operations⁴⁹. First; priority reform areas are to reduce the administrative burden of tax, improve taxpayer services, and simplify export-import procedures. The second component is to ensure a favorable foreign trade regime and eliminate barriers to trade. Thirdly; logistics, education and infrastructure upgrades. The final component pertains to strategies to attract foreign investment.⁵⁰

On the sector-level, the most important priorities of the government are tourism, ICT health, and the education sectors, which are the designated focus of targeted projects. Detailed

⁴⁷ Armenpress 2013

⁴⁸ Mgdesyan and Khachatryan 2013

⁴⁹ RA Ministry of Economy 2011

⁵⁰ Special toolset is explained in detail in *ibid*.

information about these sectors can be found in the chapter on *Sector (meso-level) Assessment*.

Turkey

Similar to Armenia's new growth paradigm, Turkey's latest (Tenth) Five-Year Development Plan emphasizes agro-food, ICT, healthcare industries, as well as health tourism.

A priority of the Turkish Government is to enhance growth and improve competitiveness of the agro-food sector. The productivity and competitiveness of SMEs in international markets will be upgraded for this purpose. Another aim of the policy is to accelerate the transition to high-value-added production of the sector.

The ICT sector is another priority area for industrial development that will play an essential role to help Turkey make the transition to a knowledge-based economy. In this respect, establishing fast and cost-effective mobile and Internet broadband services across the whole country is of utmost importance for Turkey to realize its ambitions.

In the upcoming five-year period, healthcare industry is likely to witness major growth as a result of rapid technological developments. Therefore, the government declared an increase in public expenditures on the health sector to enhance the quality of health infrastructure and health tourism services. Public expenditures will also capture the implementation and use of latest technologies for medical services in order to augment the competitiveness of the sector. Similarly—depending on each country's progress towards achieving its national development goals—economic cooperation at the regional level could yield positive outcomes. The eastern regions of Turkey already have set their own objectives to advance their educational and technological capacities, and could incorporate increased interaction with Armenia into their local policy agendas.

Turkey's eastern regions have formulated their own development plans, some of which are complementary to Armenia's sectoral priorities as they include the promotion of the tourism, healthcare, and agro-food sectors. A summary of regional development strategies is featured below.

Table 16: Development Objectives of Turkish Regions

TRA1 (Erzurum, Erzincan, Bayburt)	TRA2 (Ağrı, Ardahan, Iğdır, Kars)
<ul style="list-style-type: none"> • Strengthening the human capital & social infrastructure • Providing the environmental sustainability & improve the technical infrastructure • Increasing the capital stock & FDI • Advancement the educational and technological capacity 	<ul style="list-style-type: none"> • Improvement of the standard of living • Enhancement of the GVA & production efficiency of agricultural & husbandry production • Branding the region by realizing the potential strengths in tourism • Increasing the competitive power of firms
TRB1 (Malatya, Bingöl, Elazığ, Tunceli)	TRB2 (Bitlis, Hakkari, Muş, Van)
<ul style="list-style-type: none"> • Strengthening the human capital & social infrastructure • Enhancement of the agricultural & food sectors • Enhancement of the industry & services • Advancement of technical infrastructure • Improvement of the standard of living in rural areas • Maintenance of the environmental sustainability 	<ul style="list-style-type: none"> • Increasing the efficiency, diversity & value added in agricultural production • Activating potential sectors excluding agriculture • Enhancement human & social capital • Renovation of the urban and rural infrastructure

Concluding Remarks for Policy Framework and Institutional Assessment

Recent policy developments. Main strategies of the Armenian government that have been discussed are: Armenia’s Export-Led Industrial Policy document (2011), the National Competiveness Foundation of Armenia (NCFA), EurAsEc customs union membership, and the *Open Skies* policy. Main policy documents for Turkey are: Turkey’s latest Five-Year Development Plan and as significantly regional development policies of Turkey’s eastern parts.

Priority Mapping in Armenia – Transition to a high value economy. Armenia’s export-oriented, new industrial strategy document focuses on orienting the manufacturing industry towards high-value products. The strategy aims to have long-term, positive impact on Armenia’s export growth—which is constrained by its landlocked position—by developing expertise in a small number of niche areas and utilizing air transportation to export high value products to foreign markets. Another initiative the Armenian government took to enhance the productivity of certain domestic industries was the establishment of the National Competiveness Foundation of Armenia (NCFA) to create formal links between the Armenian business community abroad and the Government of Armenia. The NCFA aims to build a knowledge-based economy by taking advantage of the capabilities and resources of the Diaspora community to serve national development in the healthcare, education, and tourism sectors, and to provide subsidized loans and equity financing as a source for ground financing in coordination with funders from the Diaspora.

Priority Mapping in Turkey – Transition to a high value economy. Similarly, Turkey’s latest Five-Year Development Plan aims to increase the productivity and competitiveness of certain sectors. One such policy priority is the acceleration of high-value-added production in the agro-food sector by facilitating productivity and competitiveness of SMEs in international markets. A second priority is to invest in the development of the ICT sector to help Turkey make the transition to a knowledge-based economy. Another priority is to enhance competitiveness

of the healthcare industry by investing and promoting the latest technologies in medical services. The regional development policies of Turkey's eastern parts have also prioritized increasing competitiveness of businesses and the strengthening of human capital resources as well as technical infrastructure in their respective regions.

Coinciding sectoral priorities. Sectors that are major priorities of both the Armenian and Turkish national development strategies—such as the ICT, tourism, health, and agriculture sectors—create room for economic cooperation at the national level. The regional development plans of Eastern Turkey also include sectoral priorities that match Armenia's, including the promotion of the tourism, healthcare, and agro-food sectors.

FTAs and customs unions. While Turkey has had a customs union with the EU since 1995, Armenia recently announced its decision to join the Customs Union of Belarus, Kazakhstan, and Russia (EurAsEc). Armenia's EurAsEc membership is unique in that the country is joining a customs union, which has higher tariff rates than its own. Since the customs union has higher tariff rates, Armenia's membership may impose additional costs on its trade with Turkey as well as have large trade diversion effects on Armenian imports in general. One way to tackle the difficulties that may result from Armenia's membership is to apply an internal processing regime, which grants tariff and tax exemptions to imports that will be used in the production of exports. The arrangement may help Armenia and Turkey jointly access third markets.

The Policy Framework and Institutional Assessment provided the current contextual setting to accurately assess the feasibility of regional economic cooperation in sectors discussed in the previous chapters. Moreover, while the general macro-level and product-level assessments reflect present economic indicators, the sectoral and policy assessments capture evolving economic patterns and structures, and reveal opportunities for economic cooperation. The next section will identify critical opportunity areas between Armenia and Turkey based on these assessments.

3.5 Synthesis of Results: A Taxonomy of Opportunities

In this section, we synthesize the key results from the four layers of assessments in order to identify critical opportunity areas for cooperation between Armenia and Turkey. The preliminary list of sectors (See *Sector (meso-level) Assessment*) were evaluated based on four main criteria: (i) The effects of closed borders on business interaction in selected sectors; (ii) The compatibility of sectors with the policy priorities of Armenia; (iii) The compatibility of sectors with the policy priorities of Turkey; and (iv) The suitability of sectors for SMEs, e.g., assessing barriers to entry that prevent firms from entering the sector.

The first criterion is to assess the impact of closed borders on economic interaction between Armenia and Turkey. At present, the closed borders and logistical difficulties reduce the feasibility of many trade-based activities. Hence, investments in sectors and value chains that do not depend on large scale and frequent movements of commodities across borders are strategic investment areas in the short run, e.g., services sectors and high-value, small-size manufacturing products. An emphasis on services sectors and high-value products also matches Armenia's economic and labor force structure, as reflected in the prominence of the ICT sector. Moreover, Armenia is landlocked due to closed Turkish and Azerbaijani borders, which makes it difficult to trade in goods, while the export of services such as ICT is easy and low cost.

The second criterion aims to measure the compatibility of the selected sectors with Armenia's new industrial policy, which will determine the axis of Armenia's economic development until 2020. The new strategy adopted by the Armenian Government in 2011 aims to gear the country's industry towards export-oriented and knowledge-intensive sectors and products. In addition to improving the overall determinants of competitiveness—such as the business climate, financing, and infrastructure—the new industrial policy aims to develop specific sectors, including mining, metallurgy, agricultural-food production, jewelry, machine building/precision engineering, chemicals, textiles, construction materials, as well as ICT, tourism, health, and education⁵¹.

The third criterion is the relevance of the selected sectors to Turkey's current economic policy priorities. In this regard, Turkey's latest Five-Year Development Plan aims to gear the country towards a high value-added and knowledge-intensive economy by increasing the productivity and competitiveness of certain sectors, including the agro-food, ICT, and healthcare sectors. The regional development policies of Turkey's eastern parts have also prioritized increasing the competitiveness of businesses and the strengthening of human capital resources as well as technical infrastructure in their respective regions.

Our final criterion measures the concentration of SMEs and assesses sectoral barriers to entry for SMEs in selected sectors. We believe that increasing the participation of SMEs in bilateral economic relations has positive spillover effects on regional economies, and can also contribute to the sustainability of the rapprochement process between Turkey and Armenia. Conversely, a scenario where large companies are the sole beneficiaries of economic development will create legitimacy problems and limit economic growth that includes economic integration of a larger number of actors. For these reasons, we attached a great deal of importance to select SME-friendly sectors and products where SMEs do not face significant entry barriers, such as high-level capital investment and economies of scale requirements.

Based on the above criteria, the main target sectors for cross-border private sector cooperation projects are summarized in

⁵¹ RA Ministry of Economy 2011

Table 17. The ICT, tourism, and hospitality sectors stand out as presenting the highest degree of economic opportunity. The education, health, and retail sectors also offer opportunities for cooperation between the two countries, although SME participation in these sectors is limited. The energy and finance sectors require high-level capital investment and therefore are not SME-friendly sectors. The possibilities for cooperation in the transport and logistics sector are limited because of the closed border.

Table 17: Results of the Sector Assessment based on the Four Criteria

	Border problem?	Armenia Policy Priority?	SME Orientation?	Policy relevance for Turkey?
GOODS				
Primary Goods (mining)	○	●	○	○
Food and Agricultural	○	◐	●	◐
Construction Materials	○	●	◐	◐
Pharmaceuticals	◐	●	○	●
Textiles and Apparel	○	◐	●	○
Machinery and Electronics	◐	◐	◐	●
Other Man. (Jewelery etc.)	◐	◐	◐	◐
SERVICES				
ICT	●	●	●	●
Energy	●	◐	○	●
Construction and Engineering	●	◐	◐	◐
Retail	●	○	◐	○
Education	●	●	◐	◐
Finance	●	○	○	◐
Health	◐	●	◐	●
Tourism and Hospitality	◐	●	●	●
Transport and Logistics	○	◐	◐	●

Source: TEPAV Research

- : High level
- ◐ : Medium level
- : Low level

The following section introduces concrete project ideas and confidence building measures geared towards improving the competitiveness of ICT- and Tourism-related activities in Armenia and Turkey.

5 Towards a Roadmap: Project Ideas as Economic Confidence-Building Measures

In this section, we propose a new set of confidence-building measures (CBMs) to strengthen economic relations between Armenia and Turkey. The main findings in previous sections that shaped the design of CBMs can be summarized as follows:

- Although Armenia has a lower per capita income level than Turkey's eastern regions, it displays a higher degree of development in terms of human development. Furthermore, the product-level analysis shows trade complementarities between Armenia and Turkey's most developed Istanbul region (although this is largely due to the Istanbul region's diverse export basket). Trade complementarity between Armenia and Eastern Turkey, however, is very low, and the closed border further restricts the trade of goods in the region. Hence the study concludes that, in the short run, people exchange and services trade are the most viable forms of regional cooperation between Armenia and Eastern Turkey.
- Yerevan is the largest urban center in the region to the east of Gaziantep. The city holds the potential to become an attraction for Eastern Turkey's population, including cultural tourism and business- and entertainment-related visits by the upper-middle class in Eastern Turkish cities. Lastly, Yerevan and Gyumri can also become hubs for health and education services to serve Eastern Turkey's population, who are far from developed Turkish cities that offer such services.
- Third, while current industrial structures of the two sides do not presently complement each other, the future directions of both sides' industrial policies can bring a set of cooperation opportunities. Eastern Turkey is the least developed region of Turkey, with high transportation costs and a low level of human capital. This has led to industrial underdevelopment to such an extent that even large-scale public subsidies to attract investments to the region have not been able to reverse. On the Armenian side, though, skills appear to be less of a constraint: the closed borders with Turkey and Azerbaijan limit economic diversity and the range of goods that can be produced. Despite shortcomings, governments on both sides of the border have committed themselves to ambitious industrial transformation agendas. The complementary elements of each agenda can be used to have both sides move towards higher value-added activities and more advanced segments of manufacturing. The study identified health-related services and products, and tourism and ICT, as areas with considerable overlap in each side's policy agenda.
- Fourth, upon examining the sectors based on four criteria—namely, border dependence, SME orientation, and policy priority for Armenia and Turkey—we identified two sectors that present more opportunities than others in terms of facilitating business synergies. The first one is the tourism sector, which is both an area involving a great deal of SME activity and one prioritized by the governments of both sides. Furthermore, the shared historical heritage is a strong asset to enhance tourism and attract large numbers of visitors from both sides. The second sector is ICT, which is a fast-growth sector on both sides, and has the potential to boost economic productivity and generate high-quality, well-paid jobs for youth. Market complementarities, outsourcing, and joint product/service development can be important areas of collaboration between the two countries' ICT sectors.

The findings of this research helped us design tangible project ideas that can create business synergies and mutually beneficial economic outcomes. The projects have the potential to function as *confidence-building measures* between the Armenian and Turkish business sectors, as well as other critical stakeholders, such as private sector support organizations and the two countries' political and bureaucratic leadership. Furthermore, the common features guiding the confidence-building effort include the projects' purpose and political feasibility, technical correctness, and institutional capacity, as follows:

- **Purpose and Political Feasibility.** Armenian-Turkish relations are a politically thorny issue. Therefore the proposed projects aim to contribute to the rapprochement between Armenia and Turkey from an economic regional cooperation perspective. Achievements in the economic realm are expected to follow progress on the more sensitive political issues. Furthermore, project ideas geared towards generating business opportunities for SMEs are central to the effort to not only build sustainable business links, but also increase the political feasibility of projects. SME participation will allow the incorporation of a large number of diverse stakeholders into the confidence-building process and help gather public and political support for projects.
- **Technical correctness.** The project ideas are based on, and guided by, economic rationale and analyses. The design and implementation of projects to build confidence are formulated on the basis of economic analysis, which is expected to enhance the technical correctness of project proposals.
- **Operational capacity and successful implementation.** In order to ensure the success of projects, we also aim to improve the technical capacities of private sector support institutions, both at the governmental and non-governmental levels. Capacity building will strengthen the technical and administrative capacity to implement projects and CBMs.

In view of these principles we established three different types of projects that can create business synergies and contribute to the confidence-building effort. These are as follows:

- (1) **Interaction- and connectivity-focused projects.** Projects in this category specifically aim to increase the interaction between targeted groups through activities such as firm-level matchmaking initiatives, networking events to enhance entrepreneurship, and workshops for other stakeholders and key decision makers. The desired outcome of such projects is to increase the mutual awareness of core competencies and comparative advantages of both sides.
- (2) **Feasibility studies and advocacy-focused projects.** The aim of these projects is to identify creative ideas that can enhance economic integration and measure the impact and feasibility thereof. Examples of project ideas range from establishing new flight routes to building joint production zones for targeted value chains. Impact and feasibility should be carried-out using a multi-domain and multi-dimensional approach in order to capture the regional, national, and sectoral impacts of projects. Analyses of value chains should be included in the assessment, where relevant to fully reveal complementarities. Based on the findings of technical assessments, advocacy-related activities could be organized to disseminate and promote results to various stakeholders. The desired outcome is to raise awareness of the impact of further

regional economic integration in addition to providing technical support that can help transform new ideas into concrete projects.

- (3) **Capacity-building-focused projects.** Capacity-building projects will be based on the results of needs assessments for particular institutions and organizations that are critical to regional economic integration. Examples of such projects range from establishing training institutes for the tourism industry to private sector support organizations for the ICT sector. Training programs and workshops could be tailored to meet the specific needs of institutions and organizations. International organizations, such as the World Bank Institute or donor country best-practice agencies, can also be mobilized in capacity-building processes. The desired outcome of this type of project is to increase interaction at the institutional and organizational level, in addition to institutional capacity-building for effective service delivery.

In light of the proposed framework, we conclude our study with a number of project ideas that, we believe, have the potential to create a positive agenda and strengthen the path towards economic interaction between Armenia and Turkey. However, it should be noted that the following are “ideas,” as opposed to full-fledged project descriptions. For each project “idea” we present a brief note on the background and rationale of the project, a list of main project activities, the desired outcomes of the project, and potential project partners, funders and beneficiaries (relevant stakeholders).

Project Idea #1: Impact analysis for new flight routes

Background and rationale

- Potential areas of cooperation include marketing Yerevan as a destination for the Turkish upper-middle class as well as having more Armenians visit Turkey for touristic and commercial purposes. It is also possible to turn Eastern Anatolia into a tourism destination by promoting South Caucasus Tours.
- The Armenian tourism sector has been growing rapidly. The sector attracts 400,000 visitors per year from Diaspora. On the other hand, Turkey is among Armenian tourists’ top holiday destinations. In 2012, 70,000 Armenians visited Turkey—travelling to destinations such as Antalya and Istanbul, in addition to Van, Adana, Mersin, Elazığ, and Cappadocia, which are among their ancestral lands. Tours usually last between 3 and 11 days, and frequently utilize buses that travel through Georgia.
- The most important challenge facing the Armenian tourism sector is a lack of connectivity in the region. The closure of borders limits transportation possibilities to air travel alone, which is expensive and limited. The lack of an effective marketing strategy exasperates low demand and keeps prices high. Moscow and Tehran are the only cities that have direct daily flights to Yerevan’s Zvartnots Airport. However, flight frequency has already started to increase as a result of the government’s *Open Skies* policy.
- The project would focus on analyzing the potential impact of new flight routes between Armenia and Turkey, including Yerevan-Van, Yerevan-Adana, Yerevan-Bodrum, as well as increase the number of flights between Istanbul and Yerevan. For instance, travel

time from Yerevan to Van lasts as long as 22 hours by road; “How would a 30-minute flight impact the demand for travel between the two cities?”

Main Project Activities

- Stakeholder mapping and analysis for establishing new flight routes, factoring in legal, institutional, and technical issues.
- Identifying the current state and determinants of tourism; literature review on increased connectivity via flight connections on tourism; design of a methodology.
- Economic impact assessment of increased tourism (employment, revenues, entrepreneurship, etc.) via new flight routes
- Impact assessment for social, cultural, and regional development.

Desired Outcomes

- Advocacy for regional and national stakeholders on both sides, based on concrete evidence.

Relevant Stakeholders

- Tourism companies
- Airlines
- Civil aviation authorities
- Multilaterals and donors

Project Idea #2: Kars-Gyumri Special Tourism Zone Around Ani

Background and rationale

- Ani Bridge, on the Armenian-Turkish border, has significant historical importance dating back to 10th century. A tourism cluster around the Ani region can become a magnet for tourists visiting Armenia and Eastern Turkey.
- Ani possesses historical significance as Gothic Architecture was born there. It was the center of the Silk Road—connecting African, Asian and European civilizations—and is identified with World Heritage Status by UNESCO.
- Several historical and touristic attractions in Eastern Anatolia that are significant for Armenians (Çiçek Valley, Beden Gate, Sultan Palace, Apostle Church, Georgian Church, Hidrellez Gate, Abugamrents Church, Bakireler Monastery etc.).
- Similar international examples can be found (such as the Mostar Bridge) that can be inspirational for the (re)development of the Ani Bridge and Tourism Zone

- Infrastructure needs: language education; tourism and hotel management training for the local people; logistics infrastructure such as roads,
- Administrative issues: Easing entry and exit of Diaspora and Armenian citizens; enabling visa-free access for those who want to visit the specially-delimited "Ani Free Zone."

Main Project Activities

- Research for different restoration ideas and options
- Awareness-raising and gathering political support
- Producing a report on administrative, financial, technical, and legal issues and constraints
- Forming a scientific working committee
- Organizing a cultural heritage conference
- Forming an Armenian-Turkish technical taskforce and organizing its meetings
- Developing a joint governance structure for the Ani Tourism Zone

Desired Outcomes

- Improved connectivity and people-to-people connections
- Increased visits by Diaspora Armenians to Eastern Anatolia
- Increased local tourism revenues
- Economic development in Eastern Turkey and Armenia
- Recognition and restoration of key sites of historical importance

Relevant Stakeholders

- Ministries of tourism and culture of both sides
- Tourism-focused SMEs
- Local businesses that cater to the tourism value chain
- Local and regional construction companies

Project Idea #3: Joint industrial cooperation (ICT value chain and market assessment)

Background and rationale

- The ICT sector is one of the most dynamic and promising sectors of the Armenian economy. The sector boasts high number of ICT graduates and competitive labor costs.
- The IT, telecom, and engineering sectors combined contribute above 6% to Armenia's GDP (EV), while the ICT sector's contribution to GDP in India or USA is about 3% (WB). CAGR of the ICT sector between 2008 and 2011 was around 22%, whereas average annual growth rates (AAGR) of agriculture and food processing were 10.4% and 11.3%, respectively.
- ICT is also one of the top export-oriented sectors in Armenia, where the geographic location and border closures inhibit trade. The sector accounted for 8.5% of exports in

2010 (WB), while the CAGR of exports was 8.9% during the period between 2008 and 2011.

- The majority of firms specialize in Internet services, web development, and IT consulting (WB). The major players in the IT market are Synopsis, Microsoft, Credence Systems, Mentor Graphics, Armsoft, Instigate, and Cambric Armenia.
- Channeling higher-education graduates into the ICT sector and improving their training is critical. Absence of high-quality transport and office space are also important issues. There are also transparency, stability, and predictability problems in the regulatory environment, with implications on intellectual property and data protection.
- Cooperation between Turkish and Armenian ICT companies can result in mutual gains. First, both nations can develop structural cooperation. While Armenia has a highly qualified and cheaper labor force, Turkey's ICT workforce is costlier. On the other hand, Turkey has better infrastructure (office spaces, equipment etc.) and a larger ICT market than Armenia. Therefore, both countries can be better off in the ICT sector if they exchange their comparative advantages.
- Second, Turkey and Armenia can cooperate in entrepreneurship. Turkey has a better entrepreneurial environment with angel investors, accelerators, and mentors. Armenia has better human capital to deliver demanding projects. As such, bringing together Turkish mentors, accelerators, and investors with Armenian potential entrepreneurs would advance the entrepreneurship ecosystems of both countries.

Main Project Activities

- Areas that present the highest potential gains from economic cooperation can be identified through mapping and analyzing the detailed value chains of ICT activities on both sides.
- Potential linkages of Armenian ICT supply chains with major European and Turkish companies can be investigated.
- Stages where Turkish and Armenian businesses would best fit in given their capabilities, either separately or jointly, can be identified.
- Matchmaking events for companies that can complement each other in terms of target markets (e.g. Russia and US) and fields of expertise.
- Networking events such as joint start-up weekends, entrepreneurship delegations (with business angels and VC fund managers), and joint business plan contests.

Desired Outcomes

- Increased connectivity between ICT based SMEs of both sides.
- Increased marketing access, including the Turkish market for Armenian firms, and Russian, US, and CIS markets for Turkish firms.
- Joint business plan, funding, and development activities.

Relevant Stakeholders

- ICT-based SMEs
- Early-stage start-ups, and young entrepreneurs with business plan ideas
- Universities, Technoparks, Incubators
- ICT-focused NGOs and employer unions

Project Idea #4: Utilizing multilateral platforms

Background and rationale

- The fact that Turkey and Armenia failed to establish official diplomatic relations to date should not curtail the relations between two countries through multilateral platforms. These include the Black Sea Economic Cooperation Organization (BSEC), NATO, OSCE, Council of Europe, European Union, and of course United Nations.
- Given the (potential) political problems faced when implementing even simple CBMs, experience suggests that carrying the issues to multilateral platforms may have a practical value. A concrete example is about the truck permits: Turkey and Armenia do not have a bilateral transport agreement, therefore for years Turkey was not able to issue entrance permits to Armenian trucks. However, in 2012, utilizing the BSEC Black Sea Highway agreement, Turkey issued up to 200 permits to Armenian trucks. These permits are used by Armenian trucks carrying cargo to Russia through Turkey's Black Sea ports—a critical route during the harsh winter of North Caucasus.
- It is possible to explore ways of utilizing multilateral platforms for similar novel approaches to ease administrative barriers on specific economic cooperation opportunities, including aviation and trade areas.

Main Project Activities

- Exploration of opportunities primarily within the framework of, but not limited to:
 - The United Nations Convention on Transit Trade of Landlocked States, to which both Turkey and Armenia are signatories, with Armenia signing very recently in 2013 (aim: opening talks on direct transit trade within the framework of this UN convention).
 - The European Common Aviation Area, to which both Turkey and Armenia are transitioning into (aim: explore the possibility of starting regular (not charter) flights

that can connect to many other flights from Istanbul, hence increasing connectivity of Armenia).

- The World Trade Organization, to which both countries are signatories, but Turkey having a reservation about the most-favored-nation status of Armenia (aim: exploring ways Turkey can allow legal imports of Armenian goods without necessarily opening the border).
- Submission of a policy report to a workshop organized in late 2014 during the Swiss chairmanship of OSCE.

Desired Outcomes

- Increased utilization of neutral international platforms; design and implementation of more CBMs between Turkey and Armenia.
- Increased interaction between international and regional platforms, and other stakeholders.

Relevant Stakeholders

- Black Sea Economic Cooperation (BSEC)
- European Union
- Organization for Security and Co-operation in Europe (OSCE)
- North Atlantic Treaty Organization (NATO)
- Council of Europe

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