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HOW TO IMPROVE TRADE RELATIONS BETWEEN PORTUGAL AND RUSSIA

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Master in International Management

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Iscte - Instituto Universitário de Lisboa,

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BUSINESS
SCHOOL

Department of Marketing, Strategy and Operation

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Abstract

Despite the long-standing cooperation between Portugal and Russia, the current bilateral trade values do not commensurate the two and a half decades of cooperation. The current trade values trend based on data between 2006 and 2019 shows somewhat unstable trade relations characterized by both rising and falling in different years. While different scholars have explored the challenges that should be addressed, such as trade protectionism and opportunities that can be exploited to enhance trade relations, there still exists a gap in literature exploring various measures that can be employed to improve the Russian-Portuguese trade relations. Therefore, this research aims to explore the current situation in the trade relations between Russia and Portugal and also the measures that can be employed to improve the international trade standing between the two countries. Analysis of data from secondary sources shows that Portugal and Russia have traded for approximately 240 years. Russia mainly sells crude oil products and farm inputs to Portugal, while Portugal mainly provides agricultural commodities to Russia. The key success factors required to improve the Russian-Portuguese trade relations include favorable trade policies, increased foreign direct investment, and preferential bilateral agreements. Presently, there is a mismatch between Russia's and Portugal's trade policies, whereby Russia is more protectionist than Portugal.

Moreover, there is only one identifiable bilateral trade agreement whose impact on countries' trade relations is remote. The level of foreign direct investment is still low to impact trade relations between Russia and Portugal. This study proposes a three-fold strategy to improve Russian-Portuguese trade relations. Firstly, the relaxation of trade policies such as ease of trading across the border, tariffs, and economic freedom is necessary. Secondly, the nations should take measures to boost the level of foreign direct investment amongst them. Thirdly, preferential trade agreements are necessary to address the trade barriers and position the countries as strategic trade and investment partners.

Keywords*:* **International Trade, Bilateral agreements, Trade Policies, Foreign direct investment.**

JEL: N40, N44, N70, N74, M16

Resumo

Apesar da cooperação de longa data entre Portugal e a Rússia, o acordo comercial bilateral em vigor não é proporcional de parte a parte nos últimos 25 anos de cooperação. Os valores de transação comercial, relativamente aos anos de 2016 e 2019 demonstram relações instáveis de comércio caracterizadas por subidas e descidas em diferentes anos. Enquanto que alguns especialistas tenham explorado alguns dos desafios que devem ser encarados, como medidas protecionistas e oportunidades que poderiam ser exploradas para aumentar as relações de comércio, ainda existe uma disparidade na literatura no que concerne às diferentes medidas que poderiam ser tomadas para melhorar as relações comerciais entre Portugal e a Rússia. Por isso, esta pesquisa procura explorar a situação atual de comércio internacional entre os dois países e focar nas medidas que podem ser tomadas para melhorar o comércio internacional. A análise de dados de fontes secundárias mostram que o comércio internacional entre Portugal e a Rússia datam de, aproximadamente, há 240 anos. A Rússia vende maioritariamente produtos petrolíferos e matérias primas agrícolas a Portugal, enquanto que Portugal exporta produtos agrícolas à Rússia. Os fatores-chave de sucesso necessários para melhorar as relações de comércio incluem políticas comerciais favoráveis, aumento do Investimento Direto Estrangeiro (IDE) e acordos de preferência bilateral. Atualmente existe um desfasamento entre as duas políticas comerciais, de onde a Rússia denota uma postura mais protecionista do que Portugal. Além disso, é possível identificar apenas um acordo bilateral cujo impacto no comércio internacional de ambos os países é pequeno. O nível de IDE ainda não é suficiente para ter impacto no comércio internacional entre os dois países. Este estudo propõe uma estratégia de três etapas para aumentar as relações russo-portuguesas: em primeiro lugar, é necessário a flexibilização de políticas comerciais, como, por exemplo no sentido de facilitação de comércio bilateral, tarifas e liberdade económica; em segundo lugar, as nações deveriam tomar medidas para aumentar os níveis de IDE; por fim, acordos de comércio preferenciais são necessários para enfrentar as barreiras comerciais e posicionar os países como parceiros estratégicos de comécio e de investimento.

Palavras-chave*:* **Comércio Internacional; Acordos bilaterais; Políticas comerciais; Investimento direto estrangeiro (IDE).**

JEL: N40, N44, N70, N74, M16

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1. Introduction

Portugal and Russia have a long-standing fruitful relationship in international trade where both countries import from and export to each other. According to the Russkiy Mir Foundation (2018), Portugal and Russia's bilateral relationship dates back to over 240 years. According to United Nations COMTRADE data, Russia's total value of imports amounts to $ 254 billion, approximately 15% of the annual GDP, while Portugal's imports amount to $ 89.92 billion, approximately 38% of the annual GDP. On the other hand, Russia exports $418 billion worth of goods and services, estimated at 25% of the GDP. In comparison, Portugal exports $67 billion worth of goods and services estimated at 28% of the GDP (United Nations, 2019).

	Russia	**Portugal**
Imports ($ Billion)	254.05	89.92
Imports % of GDP	14.94%	37.81%
Exports ($ Billion)	418.80	67.00
Exports % of GDP	24.63%	28.21%
Trade Balance	164.74	-22.86
Trade Balance % of GDP	9.69%	-9.60%

Table 1: Portugal and Russia foreign trade comparison (United Nations, 2019)

(The table summarizes the imports and exports value in USD billion, also expressed a percentage of the respective countries' GDP. The trade balance reflects each country different between the exports and imports; positive value shows a surplus while a negative value shows a deficit)

Portuguese-Russian trade relations have fundamentally been founded on constructive interaction, mutual respect, and partnership (Shcherbak, 2018). According to Shcherbak (2018), Portugal is one of Russia's most crucial European partners. Among the important areas of Portuguese-Russian relations includes economic and trade relations as well as cultural cooperation activities.

Both Russia and Portugal are key players in the world's international trade. According to (OECD 2020), Russia's top export commodities include petroleum (gas, refined petroleum, and crude petroleum), wheat, and coal briquettes. On the other hand, Russia is a major importer of packaged medicaments, vehicle parts, spacecraft and planes, and cars. Portugal mainly exports uncoated paper, leather footwear, refined petroleum, vehicle parts, and cars. Portugal's main imports include petroleum gas, crude petroleum, cars, vehicle parts, and packaged medicaments (EOCD, 2020).

1.1 Problem Statement

Despite the decades of fruitful cooperation between Portugal and Russia through international trade, various aspects can be addressed to boost international trade activities between the two countries. According to Sputnik International (2017), several unfulfilled trade opportunities exist that Russia and Portugal can exploit to deepen international ties between them. The opportunities exist in services such as software and tourism and goods such as luxury goods, agricultural products, machinery, and tools (Sputnik International, 2017). For instance, Portugal is the second leading manufacturer and exporter of luxury goods in the world. On the other hand, Russia is a promising luxury goods market.

The 2019 export data published by the United Nations in the COMTRADE database corroborates the argument by Sputnik International explored above. Portugal’s export data shows that Russia ranked 42nd in Portugal’s export market by dollar value. On the other hand, Portugal ranks 12th in Russia's export market by dollar value (United Nations, 2019). Based on the data, it is evident that Portugal is yet to maximize its trading potential in the Russian market. Similarly, Russia can exploit more opportunities in Portugal to rank among the top ten exporters in future periods.

While different scholars have highlighted the various opportunities that can be exploited to deepen international trade relations between Russia and Portugal, there is still a gap in the two trading partners' measures to improve bilateral trade. This paper focuses on addressing how Portugal and Russia can improve bilateral trade relations to boost international trade.

2. Literature Review

2.1 What is International Trade?

International trade encompasses the transfer of services and goods from one individual to another (Hayes, 2019), mainly through imports, exports, and enters pot trade (Feenstra, 2015). The scope of trade encompasses two or more parties in individuals, organizations, regions, or countries. International trade takes place between two or more countries (Hayes, 2019). Bilateral trade occurs between the two countries, while multilateral trade involves more than two countries (Feenstra, 2015). International trade allows consumers in different countries to access goods and services that are not produced or available in the consumers' countries, and goods and services that would be too expensive to acquire domestically. On the other hand, some scholars have argued that international trade is not entirely beneficial to all countries (Mansfield and Reinhardt, 2015: 84.). For instance, international trade has been criticized for having adverse effects on smaller countries, especially exposing them to exploitation by stronger countries at the global markets.

The scope of trade encompasses two or more parties (Hayes, 2019). The parties can be in the form of individuals, organizations, regions, or countries. International trade takes place between two or more countries. Bilateral trade occurs between the two countries, while multilateral trade involves more than two countries (Feenstra, 2015). International trade allows consumers in different countries to access goods and services that are not produced or available in the consumers' countries, and goods and services that would be too expensive to acquire domestically. The significance of international trade gained recognition earlier on among scholars such as David Ricardo and Adam Smith (Feenstra, 2015). On the other hand, some scholars have argued that international trade is not entirely beneficial to all countries (Mansfield and Reinhardt, 2015, 84.). For instance, international trade has been criticized for having adverse effects on smaller countries, especially exposing them to exploitation by stronger countries at the global markets.

According to Feenstra (2015), international trade can be divided into import trade, export trade, and enter pot trade. Export trade encompasses goods and services sold in the international market. On the other hand, import trade refers to goods and services purchased at the international markets. Enter pot goods represents a special category of international trade where goods are imported into one country and exported to another country after value addition and modifications. Now, to a great extent, what entails international trade has been addressed. However, it is also important to answer the question of why foreign trade exists.

2.2 International Trade Theories

Classical Theories of International Trade

2.2.1 Mercantile Theory

Krugman et al. (2018) highlight that mercantilism represents the earliest international trade theory. The fundamental argument advanced by the mercantilism theory is the idea that the amount of gold and silver holdings determines a country’s wealth (Vaggi and Groenewegen, 2016). To boost a country's gold and silver reserves, mercantilism advocated for prioritizing exports over imports. Therefore, countries believed that they needed to sell more to other countries than imported from them, and consequently receive more silver and gold than they paid out.

According to Viner (2016), mercantilism requires a country to maintain a trade surplus, i.e., exports' value in terms of the reference currency is more than the imports' value. A reverse situation would constitute a trade deficit, i.e., a situation where imports' value exceeds the exports' value. Viner (2016) further argues that trade surplus and deficit concepts still exist in the modern international trade scene as countries try to maintain a surplus in the current account. Countries like Germany, Taiwan, Singapore, China, and Japan still practice neo-mercantilism, whereby exports are encouraged, and imports are discouraged (Gandolfo, 2014).

Mercantilism theory has been criticized for contributing to protectionism (Williams, 2019; 683). Williams (2019) argues that in order for a country to promote exports and discourage imports, it has to put in place various measures that discourage free trade. In modern times, different countries have implemented various protectionist policies to safeguard local industries. Cleaver (2014) highlights that protectionism embedded in import restriction policies hurts consumers and other companies as it inflates prices charged on goods and services. Also, the taxpayers shoulder the burden of subsidies accorded select exports. Therefore, mercantilism promotes some sectors to the detriment of others, contrary to free trade's fundamental tenets.

2.2.2 Absolute Advantage Theory

The absolute advantage theory emerged in 1776 (Krugman et al., 2018). Smith (2010), in the wealth of nations, questioned the mercantile theory focusing on the causes and the nature of how nations accumulate wealth. According to Krugman et al. (2018, if a country X can produce certain goods and services in a more efficient way than Y, country X have an absolute advantage. Contrary to the mercantile theory tenets of promoting exports through subsidies and restricting imports through protectionism, Adam Smith advocated for non-interference of trade though government intervention and policies Smith, (2010).

The absolute advantage theory calls for specialization (Lane and Milesi-Ferretti, 2018: 189). For instance, in a hypothetical situation, if country X can manufacture certain goods and offer certain services more efficiently than country Y, country X should specialize in producing such goods and services. On the other hand, country Y should focus on producing goods and services it can produce more efficiently than country X. Through specialization, both countries can gain various advantages such as a highly specialized workforce, increased productivity, and high efficiency and reduced efficiency production costs.

The absolute advantage theory provides a roadmap for promoting international trade far better than the mercantile theory (Chen, 2015). Specialization promotes efficiencies and encourages countries to trade to sell their products to other countries and purchase what is produced more efficiently. Consequently, the absolute advantage theory advocates measuring a country's wealth primarily by the people's living standards and not gold and silver reserves advocated by the mercantile theory.

2.2.3 Comparative Advantage Theory

While the absolute advantage theory offered a practical approach to international trade, it is limited in the application based on two core issues. Firstly, some countries possess the ability to produce more than one commodity more efficiently than other countries, and secondly, other countries do not possess any form of absolute advantage (Krugman, Melitz and Obstfeld, 2018). For instance, if country X has an absolute advantage in producing more than one commodity, whereas country Y has not useful absolute advantage, specialization may not be possible for country Y.

In response to the challenges, David Ricardo suggested a more hybrid approach to absolute advantage known as a comparative advantage (Feenstra, 2015). Comparative advantage postulates that under the circumstances where a nation is not able to make a commodity better than another country, locally, it can still produce a certain good more efficiently than other commodities. Therefore, if country Y referred to earlier have no absolute material advantage, it can still specialize in producing commodities that can be produced more efficiently than others within the country.

The comparative advantage theory offers a better international trade approach than the absolute advantage theory, as argued by (Ciuriak et al., 2015) and (Feenstra, 2015). Conversely, Porter (2011) contradicts the perceived benefits of comparative advantage, citing that in a real-world economy, the trade relations among countries stretch further than a simplistic and theoretical country X and country Y relationship. Other factors also affect international trade in the real world, such as transport and distribution, storage, and trade barriers (Gandolfo, 2014).

2.2.4 Heckscher-Ohlin Theory

According to Krugman et al. (2018), theories advanced by Ricardo and Smith suffered certain limitations that affected the advancement of countries and international trade. One of the limitations has been cited as a failure to help economies decide which commodities if produced, would help a country gain an advantage in international trade (Bajona and Kehoe, 2010). Another limitation has been cited as the general assumption that a free market would naturally help countries identify which commodities countries would produce more efficiently than others (Krugman et al., 2018).

In response to the challenges with earlier theories, the Heckscher-Ohlin theory postulates that a country can gain competitive advantage by utilizing factors of production in abundant supply within the country, e.g., such as capital, labor, or land (Krugman et al., 2018). By invoking the forces of demand and supply, the Heckscher-Ohlin theory argues that a factor of production in abundant supply would be cheaper. In contrast, a factor of production in abundant demand would cost more. Therefore, a country can leverage production factors in abundant supply, hence cheaper in production and export commodities. On the other hand, countries would be motivated to import commodities whose production factors are in limited supply and hence more expensive to produce (Krugman et al., 2018).

Modern Theories of International Trade

According to Krugman et al. (2018), the classical international trade theories could not explain the emerging trends in international trade post World War II. The two monumental developments characteristic of international trade that led to the emergence of modern international trade theories include the growth and expansion of multinational corporations and Intra-industry trade (Dieterle, 2013). For instance, the country-based theories could not explain international trade involving similar commodities. For instance, Germany sells Mercedes Benz automobiles to Japan and buys Toyota vehicles from Japan. On the other hand, Japan buys Mercedes Benz models and sells Toyota models to Germany.

2.2.5 Country-Similarity Theory

Linder responds to the classical theories' challenges in explaining new developments in international trade by advancing the country's similarity theory. According to Krugman et al. (2018), Linder argues that countries experiencing the same development level tend to exhibit similar tastes and preferences. Fundamentally, companies focus on production for the domestic markets. In the case of a surplus, countries seek export markets by seeking similar countries to the domestic market in tastes and preferences, since such markets provide the best opportunities for international trade (Feenstra, 2015).

According to the country similarity theory, it can be argued that international trade based on manufactured goods primarily takes place between nations that have similarities in aspects such as per capita income. Consequently, factors such as product reputation and brand names, customer loyalty, and quality of goods and services can be contextualized in international trade.

2.2.6 Product Life Cycle Theory

This theory emerged from the marketing field as advanced by Harvard Business School professor Raymond Vernon (Achinivu et al., 2017). According to Achinivu et al. (2017), products traded in domestic and foreign markets exhibit distinct stages, including the invention of a new commodity, the maturity of the product in the market, and standardization of the product. The product life-cycle theory is premised upon assuming that the products are innovated and manufactured to completion in the home country.

However, as observed in the case of enter pot trade, some goods do not follow a similar production (Krugman et al., 2018). Similarly, the product life-cycle theory has not provided sufficient justification for the global stage's current trade patterns. For instance, MNCs engage in product research and development in relatively low-cost jurisdictions.

2.2.7 Global Strategic Rivalry Theory

The emergence of rivalry theory can be traced back to the 1980s, mainly the studies done by Kelvin Lancaster and Paul Krugman (Krugman et al., 2018). The theory is centered on multinational corporations and their efforts to achieve a competitive advantage over other players in the same industries. Krugman et al. (2018) argue that due to the stiff competition experienced by multinational corporations in the market, the firms must develop competencies that can serve as competitive advantages. For instance, barriers to entry into certain markets or industries serve as an effective and sustainable way of firms gaining a competitive advantage over firms that seek to enter the market or industry. Some of the barriers to market entry that can give a firm a competitive advantage includes exclusive control over a key resource, distinctive production processes and industry experience, economies of scale, intellectual property rights to a product, process and distribution channels, and research and development (Ciuriak, Dan, et al., 2015).

2.2.8 Porter's National Competitive Advantage Theory

Porter's modern international trade theory represents the evolution of international trade theory in the 1990s (Krugman et al., 2018). The theory postulates that a country's prowess in international trade is dependent on the capacity to upgrade and innovate in the concerned industries (Porter, 2011). Therefore, it can be argued that some countries are more competitive in specific industries because of continuous innovation and upgrading. Porter identifies four dominant factors that help explain the theory.

Firstly, Porter (2011) identifies local market capabilities and resources, which points to a country's resources, such as available labor and natural resources. Porter (2011) argues that the commodities a country exports or imports are determined by its resources. In addition to the fundamental production factors, Porter (2011) also focuses on other factors known as advanced factors such as infrastructure, technology, education, and skilled labor. These advanced factors constitute the basis for a country's competitive advantage in international trade.

Secondly, Porter (2011) recognizes the local market demand as a crucial determinant of a country's competitiveness. Fundamentally, a country's domestic market should exhibit an adequate sophistication level to drive innovation and, hence, sustainability in the global market. For instance, multinational companies whose domicile markets are demanding, trendsetting, and sophisticated are characterized by high innovation levels in the development of new technologies, services, and products. An example of a sophisticated domestic market is the United States software market. As a result, continuous innovation and improvement are characteristic of American multinationals (Krugman et al., 2018).

Thirdly, Porter (2011) recognizes the crucial role played by the presence of complementary industries and local suppliers of inputs needed to produce commodities. Krugman et al. (2018) argue that the presence of efficient and strong supporting industries is necessary for firms to remain competitive in international trade. (Viner, 2016) highlights that, to create synergy and boost productivity, different industries cluster in certain regions endowed with support industries and supplies.

Lastly, firm characteristics determine competitiveness in foreign markets—local firm characteristics encompass competition in the industry, infrastructure, and firm strategy. A good combination of firm-specific characteristics spurs competitiveness driven by innovation (Porter, 2011).

3. Factors that May Improve Trade Relations

3.1 Trade Policy

According to Hall (2018), trade policies can either act as a barrier or a promoter of international trade. The main aspects of trade policies include tariffs, duties, import quotas, and subsidies (Hall, 2018). According to a report published by the Organisation for Economic Co-operation and Development (OECD), trade policies directly influence the market size for firms' output and impact domestic and foreign trade and investment (OECD, 2016). According to Hall (2018), restrictive trade policies that impose trade barriers affect how much goods and services a country can import or export. Therefore, eliminating trade barriers is paramount to the improvement of trade between and among foreign trade partners.

Different countries implement policies to boost exports and limit imports (Krugman et al., 2018). Research shows that restrictive policies, e.g., subsidies for exports and high tariffs on imports, impact the relative prices of the services and goods, making it either less or more attractive to export or import (Hall, 2018). Industries that benefit from government subsidies experience lower production costs, which in turn boosts production for trading in the local and international markets. Therefore, industries with subsidy allocations may be more motivated to produce for export than industries with no subsidies. On the other hand, import quotas limit the number of import goods, a firm or country can receive, which consequently raises the prices and suppresses demand. Elimination of unnecessary import quotas is a crucial avenue to boost demand for imported products. Maluck et al. (2018) corroborates Hall's (2018) findings and further observe that eliminating trade barriers promotes both international trade and the trading parties' economies.

Moreover, Hall (2018) highlights that restrictive trade policies such as import limitation through high tariffs, though they may serve to protect budding local industries, hurts international trade. For instance, it has been observed that countries with high import limitations have a relatively larger balance of payments compared to countries that have more relaxed import duties and tariffs. Evenett (2019) highlights the mistake associated with protectionism as being focused on one type of international trade (mainly goods), with the one-directional flow (import trade), and using a limited form of policy (tariffs). The government's tendency to switch between policies that favor the local firms further makes protectionism unattractive for international trade. Fundamentally, all government’s unilateral actions are geared towards favoring local interests and consequently discriminates against foreign firms. To boost international trade, it is critical to inculcate the implementation of trade policies that promote balanced competition in the market. However, protectionism alters the market conditions hence making it unattractive to foreign firms who may perceive protectionism as discriminatory (Evenett, 2019).

3.2 Bilateral Trade Agreements

Bilateral trade agreements encompass contractual agreements between trading countries, characterized by trade concessions that entail trade privileges. Such privileges exempt the trading partners from the trade barriers generally applicable to other countries. The main bilateral agreements' main contents include ease of market access, reduced quotas, and reduced tariffs Maluck et al. (2018).

Maluck et al. (2018) highlight the increasing prevalence of bilateral trade agreements in number and economic relevance. Bilateral trade agreements have increasingly gained recognition as a useful tool for deepening international trade relations between countries. While bilateral agreements involve two countries, the effect of such agreements has a spiraling effect in reorganizing trade flows that affect both the contracting economies as well as other countries that are indirectly or directly involved in international trade with the subject countries (Maluck et al., 2018).

Various past empirical studies exploring the impact of bilateral agreements on international trade (Kohl, 2014; Egger and Larch, 2011; and Zhang et al., 2017) have highlighted the positive effect of bilateral trade agreements. Zhang et al., 2017 highlighted that bilateral agreements between China and Belt and Road countries could improve international trade figures between China and the trading partners by 34%. The study by Kohl (2014) on bilateral integration of trade flows shows that bilateral agreements can improve trade figures between countries by 50%. Egger and Larch (2011) study the impact of bilateral agreements on the welfare, GDP, and bilateral trade established that bilateral agreements improve the three factors in the respective countries involved in the bilateral contracts.

In order to fully realize the benefits of bilateral trade agreements, Maluck et al. (2018) point to the cost involved in shifting production and processes to align with more efficient suppliers in other countries. According to Maluck et al. (2018), bilateral agreements' benefits do not automatically accrue to the contracting parties. Moreover, Maluck et al. (2018) highlight that bilateral trade agreements can either reinforce or weaken trade relations (especially for other countries outside the bilateral agreement) depending on the implementation strategy. This finding supports an earlier finding by Kohl (2014), which highlighted that more than half of bilateral trade agreements do not achieve the intended purpose of spurring trade between the contracting parties. Only a quarter of the bilateral trade agreements were observed to promote international trade (Kohl, 2014). Kohl (2014) associates such variations to involvement in the larger world trade organization and each country's trade institutional matters.

Another crucial factor that directly impacts bilateral agreements' success is the commitment of the contracting parties to the pacts agreed upon (Dür et al., 2014). Maluck et al. (2018) point to the complex nature and design of the bilateral agreement content, which, if not well attended to, may end up not being realized. Usually, bilateral agreements meet more than one objective and often contain the contracting nations' political interests, which can sometimes be hard to interpret in the drafting stage. However, once the agreements have been finalized, it is common to find contracting parties pulling back once the other party's various political motivations become privy to them Maluck et al. (2018).

3.3 Foreign Direct Investment

There exists a complex relationship between trade and investment, contrary to the commonly held perspective that international trade and foreign direct investment investments are loosely interdependent. There exist crucial interdependencies between foreign direct investment and trade. Firms combine investment and trade to organize services to consumers, access market knowledge, gain entry into new markets, and acquire inputs (OECD, 2020). Therefore, stimulating foreign direct investment is arguably a crucial factor that can improve trade relations between foreign trade partners.

According to Escaith (2017), though international trade has benefited greatly from global value chains, there still exist major challenges regarding accumulation distortions and restrictions of international trading costs. Such costs and restrictions negatively impact the flow of international trade among countries hence affecting both the global and local economies. Therefore, as an OECD (2020) report on the trade and investment highlights, multinationals’ investments within the trading partners' borders serve a great deal to eliminate the trade barriers and costs.

The OECD (2020) report on trade and investment further highlights that investment is no longer a binary choice for countries and firms engaging in international trade. Existing research highlights that trading and investment are mutually inclusive (Krugman et al., 2018). However, the OECD (2020) report highlights the differences across different sectors that firms and nations must consider to boost trade. For instance, banking and food industries require foreign direct investment more than sectors such as ICT and automobiles industries than heavily rely on trading. Other industries, such as internet services, footwear, and apparel, require a combination of both trade and investment.

4. The Existing Trade Relations Between Russia and Portugal

4.1 Traded Since When?

Relations between Portugal and Russia emerged in the last quarter of the 18th century (Nailia, 2017). However, the history of the relations between the countries shows intermittent cooperation characterized by interruptions and establishment from time to time until the 1980s. The key development that can be attributed to the modern trade relations between Russia and Portugal is the joining of NATO and European communities in 1986 by Portugal. As a result, the two countries obtained a formal basis upon which they would establish solid trade relations in the 1990s. Between the 1990s and 2000s, Portugal and Russia's international trade relations expanded, characterized by the signing of various bilateral treaties such as the 1994 Treaty of Friendship and visits by heads of states (European Values Center for Security, 2020). However, in the years following the global financial crisis of 2008-2009, the international trade relations between Portugal and Russia show mixed results of an increase and decrease in international trade values.

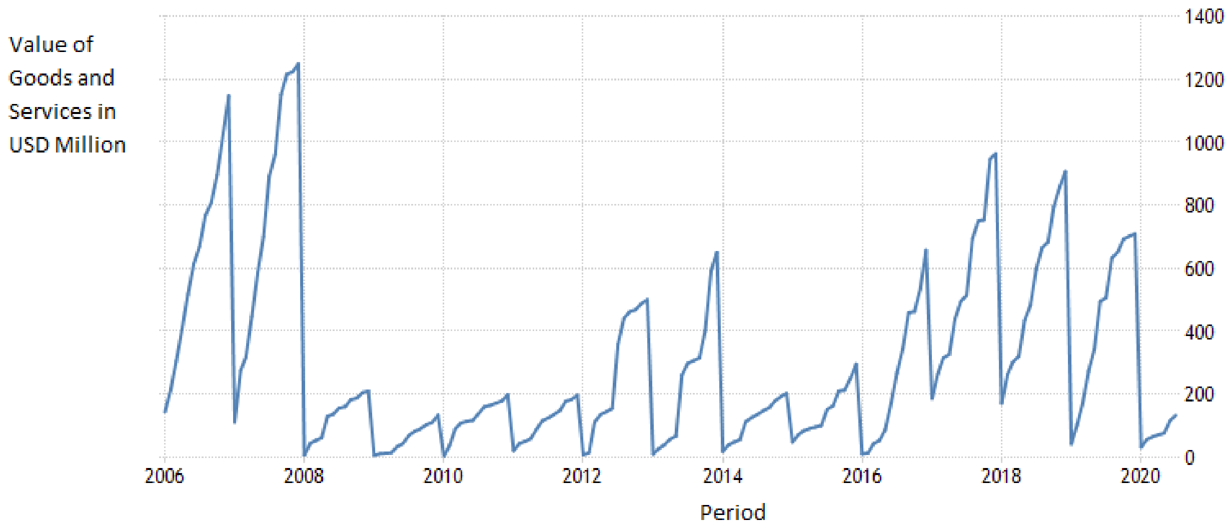

Figure 1: Russia Exports to Portugal (United Nations, 2020)

(The trend shows the trade export value in USD million from Russia, also identified as Portugal's imports from Russia. The 15-year trend data is obtained from the UN COMTRADE database.)

Figure 1 above shows Russia's exports to Portugal/Portugal's imports from Russia for fifteen years. The trend reveals that the peak of trade relations was realized before the 2008-2009 financial crisis. Post the global financial crisis, the trade relations stalled, signaled by low trade values, which remained significantly low until 2015-2016. The recovery attained after 2015 can be attributed to Portugal's change in political power, which led to the opening up of the Portuguese international markets towards Russia. Based on the trade statistics, Russia is yet to fully recover the Portuguese export market share previously attained before the global financial crisis.

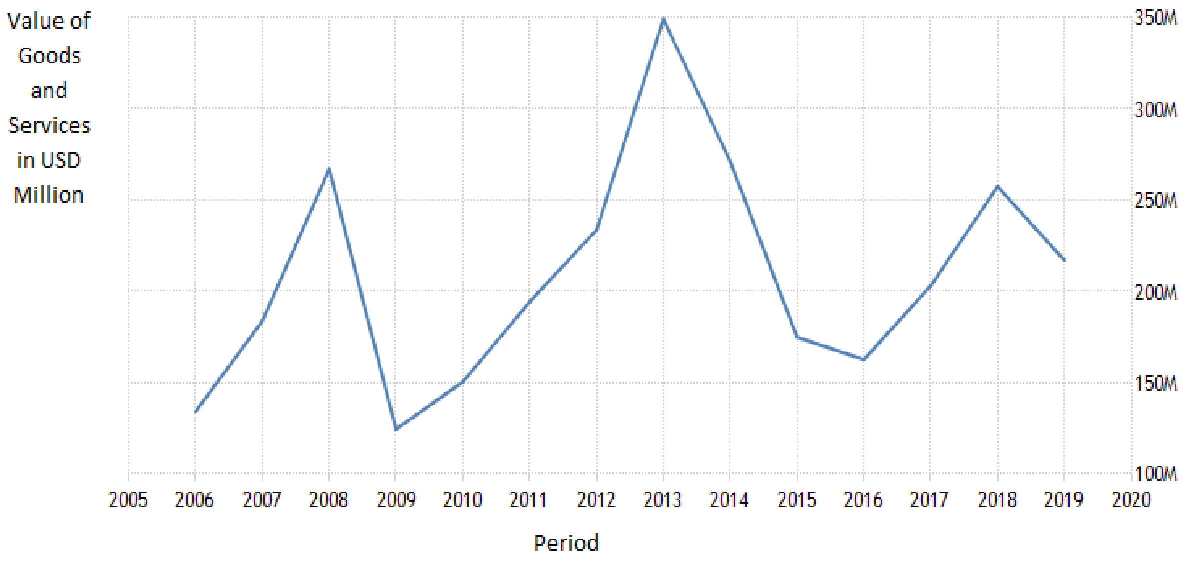

Figure 2: Portugal exports to Russia (United Nations, 2020)

(The trend shows the trade export value in USD million from Portugal to Russia, also identified as Russia's imports from Portugal. The 15-year trend data is obtained from the UN COMTRADE database.)

Figure 2.0 above depicts a trend of Portugal's exports to Russia/Russia's imports from Portugal. The trend generally shows a rise in international trade relations between 2006 and 2013. Conversely, the period between 2013 and 2019 shows a declining market for Portugal's exports in Russia. Despite the mending of the relations between Russia and Portugal post-2015, there is no effect on Portugal's exports to Russia; only a slight increase between 2016 and 2017 can be picked, but immediately followed by a sharp decline.

4.2 What Products Being Traded Now?

Portugal's imports constitute a wide range of products from Russia. According to 2019 data, the top fifteen products according to the dollar value Russia exports to Portugal are illustrated in Table 2.0 below, including the respective dollar value (Only goods worth over USD 900K are included). Other products Russia sells to Portugal include electronic and electrical equipment, metals such as copper and aluminum, plastics, footwear, apparels, glassware, vehicles, aircraft, spacecraft, soaps, pharmaceutical products, cereals, lubricants, minerals such as cement, lime, plaster, stone, earth, sulfur, and salt (United Nations, 2019).

	Top 15 Portugal Imports From Russia	**Value**
1	Fossil Fuel (Distillation products, refined fuel, and oils.	$895 M
2	Aquatic invertebrates, mollusks, crustaceans, fish	$98 M
3	Chemicals (Organic)	$88 M
4	Steel and Iron	$57 M
5	Wood charcoal, articles of wood, and wood	$22 M
6	Rubber	$18 M
7	Isotopes, metal compounds, Inorganic Chemicals	$16 M
8	Boards and paper, articles of pulp, paperboard	$8 M
9	Fertilizers	$6 M
10	Animal fodder, wastes of food industry, Residues	$2 M
11	Boilers, Nuclear reactors, machinery	$2 M
12	Sports requisites, games, toys	$2 M
13	Prefabricated buildings, lighting signs, Furniture	$1 M
14	Fruits, seed, grain, oilseed	$1 M
15	Leather, raw hides and skins	$923.88K

Table 2: Russia exports to Portugal (United Nations, 2019)

Russia's imports constitute a wide range of products from Portugal. According to 2019 COMTRADE data, the Portuguese top twenty-six products exported to Russia according to the dollar value are illustrated in Table 3.0 below (Only goods worth over USD 1 million are included). Other major Portuguese exports to Russia include fertilizers, cereals, tools, boats and ships, cocoa, glassware and glass products, metals, works of art, books, watches and clocks, carpets, musical instruments, among others (United Nations, 2019).

	Russia Imports From Portugal	**Year**
1	Articles of Cork & cork	$42 M
2	Boilers, nuclear Reactors, Machinery	$29 M
3	Footwear	$20 M
4	Fruits and vegetables	$18 M
5	Animal products	$17 M
6	Prefabricated buildings, lighting signs, and Furniture	$13 M
7	Vinegar, spirits, and Beverages	$7 M
8	Plastics	$7 M
9	Steel and Iron articles	$5 M
10	Food products, honey, eggs, dairy products	$5 M
11	Spices, mate, tea, and coffee	$5 M
12	Ceramic products	$4 M
13	Electronic and electrical appliances	$4 M
14	Paperboard and paper products	$4 M
15	Minerals (mica, asbestos, cement, plaster, stone)	$3.5 M
16	Vehicles	$3 M
17	Chemicals (Organic)	$2.9 M
18	Pharmaceuticals	$2.7 M

19	Apparel products	$2 M
20	Textiles	$2 M
21	Charcoal, wood, and wood products	$2 M
22	Vegetable and animal oils and fats	$2 M
23	Inorganic chemical products	$1.5 M
24	Cordage, twine, yarns, nonwovens, felt, wadding	$1.5 M
25	Medical apparatus	$1 M
26	Rubber	$1 M

Table 3.0: Portugal Imports from Russia/Russia exports to Portugal (United Nations, 2019)

4.3 Technological Advancement

Assessment of Russia and Portugal's technological advancement is based on the IMD World index. The index focuses on a country's ability to create and exploit innovations, develop new technologies, and technological knowledge (IMD World, 2020). Though Portugal is more apt technologically than Russia as per the ranking, the two countries have a unique opportunity to share technologies and improve trade relations.

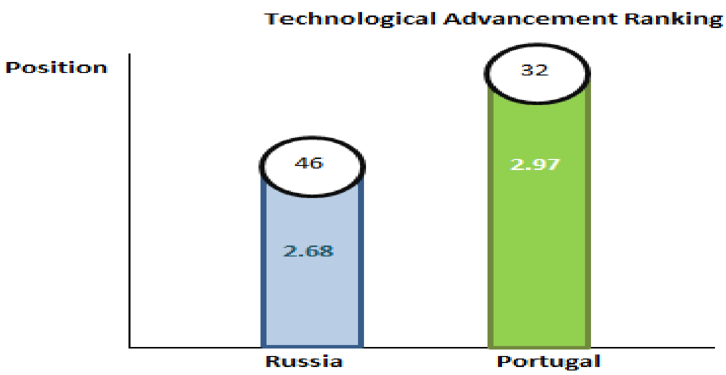

Figure 3: Russia and Portugal Technological advancement (IMD World, 2020)

(The figure shows Russia's and Portugal's technological advancement index based on the IMD index based on the country level of innovations and technological knowledge. Russia's score is 2.68 and ranked 46th globally. Portugal's score is 2.97 and ranked 32nd globally)

4.4 Russia and Portugal Competitiveness in International Trade

The comparative competitiveness was examined through the competitiveness index in the foreign markets. A comparison of Portugal’s and Russia’s competitiveness in the global market for the past 15 years is depicted in figure 3 below. Generally, Russia has been more competitive than Portugal between 2006 and 2015. This finding coincides with the higher Russia's export values compared to Portugal's. Between 2006 and 2014, both countries' competitiveness was on the rise, followed by a sharp decline from 2014. Based on the last five years average, Portugal has been more competitive in the global market than Russia. Considering bilateral trade between Russia and Portugal, comparative competitiveness is an enabling factor for improving trade between Russia and Portugal since none of the countries has a significant comparative advantage.

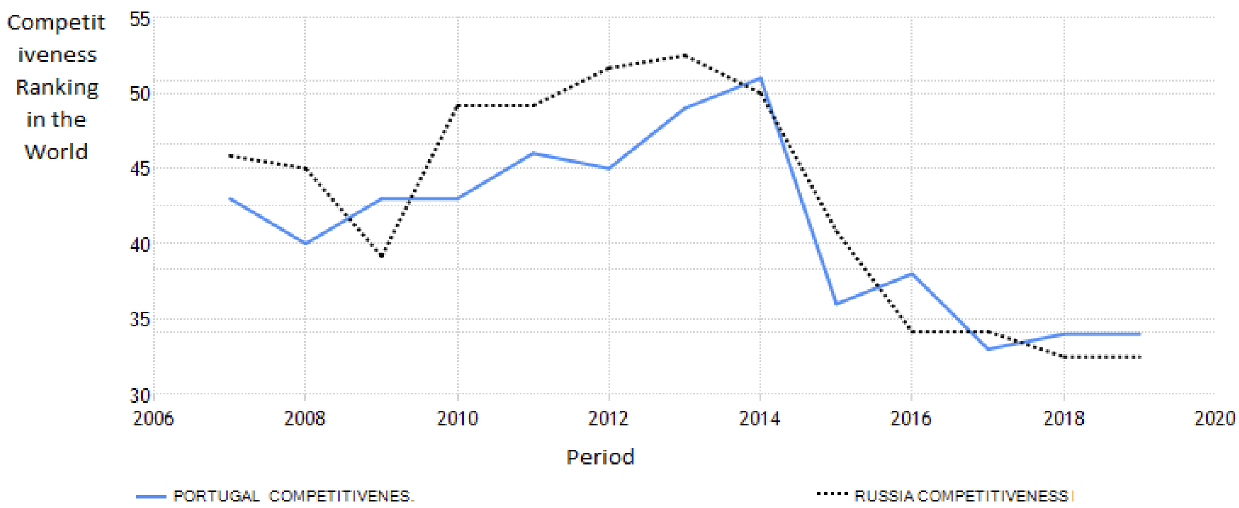

Figure 4: Country Competitiveness in Global Trade (United Nations, 2019)

(The figure shows Russia’s and Portugal’s competeviness index based on the UN COMTRADE database ranking. The Y-axis represents the respective countries’ global ranking while the X-axis shows the respective period)

4.5 Trade Policies

In this study, the existing trade policies in Russia and Portugal were examined through two measures; ease of trading in the global market, economic freedom, and tariffs.

Figure 4 below depicts a comparison of the ease of trading across borders for Russia and Portugal. Overall, Russia ranks 99th, while Portugal ranks 1st out of 190 countries in the global market. Among the factors considered in the World Bank Ranking includes ease of border compliance, export costs, the time needed to export, and documentary compliance. Improving trade relations, therefore, calls for a relaxation of international trade barriers in Russia.

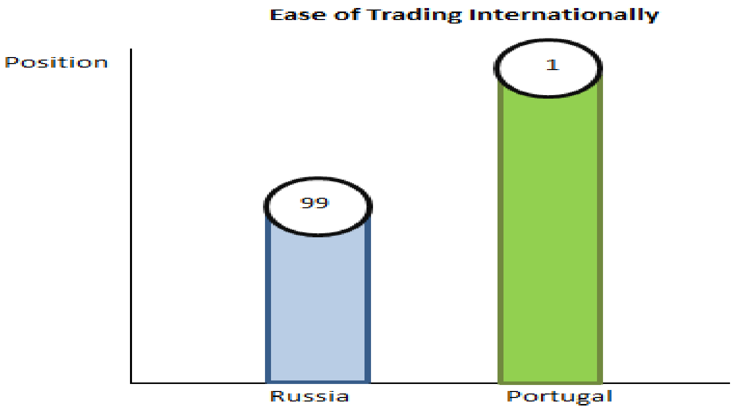

Figure 5: Ease of Trading Across Borders (World Bank, 2020)

(The figure shows Russia's and Portugal's position on the ease of trading cross-borders. The ranking is based on World Bank's analysis of various factors in the respective countries such as time taken to process export documents, the documents required, trade restrictions, among other factors)

The level of rigidity or freedom in trade policies in a country can be assessed through economic freedom data (Ott, 2018). The analysis focuses on factors such as the rule of law, efficiency of the regulations, and open markets.

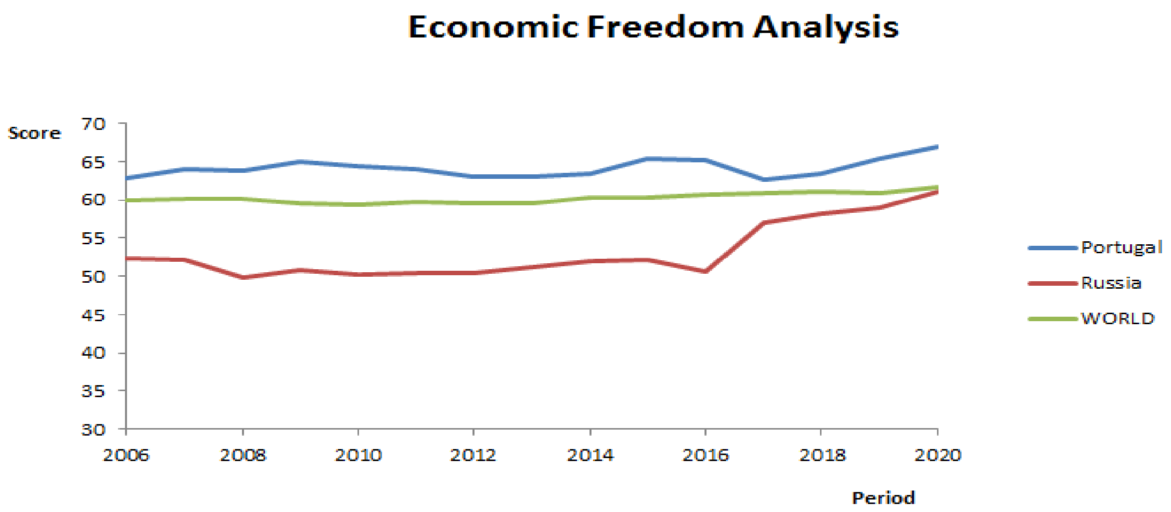

Figure 6: Economic Freedom Analysis (The Heritage Foundation, 2020)

(The figure shows Russia's and Portugal's economic freedom trend analysis based on Heritage Foundations' scores. The analysis takes into account rule of law, efficiency of the regulations, and open markets. The green trend line represents the world's economic freedom average)

Figure 5 above shows that, historically, Russia's economic freedom has been below the world average while Portugal's index has been above the world average. Therefore, Portugal's trade policies have been more liberal than Russia between 2006 and 2020. Improving trade relations between Russia and Portugal requires significant economic freedom in Russia to stimulate free trade and attract more foreign direct investment from Portugal.

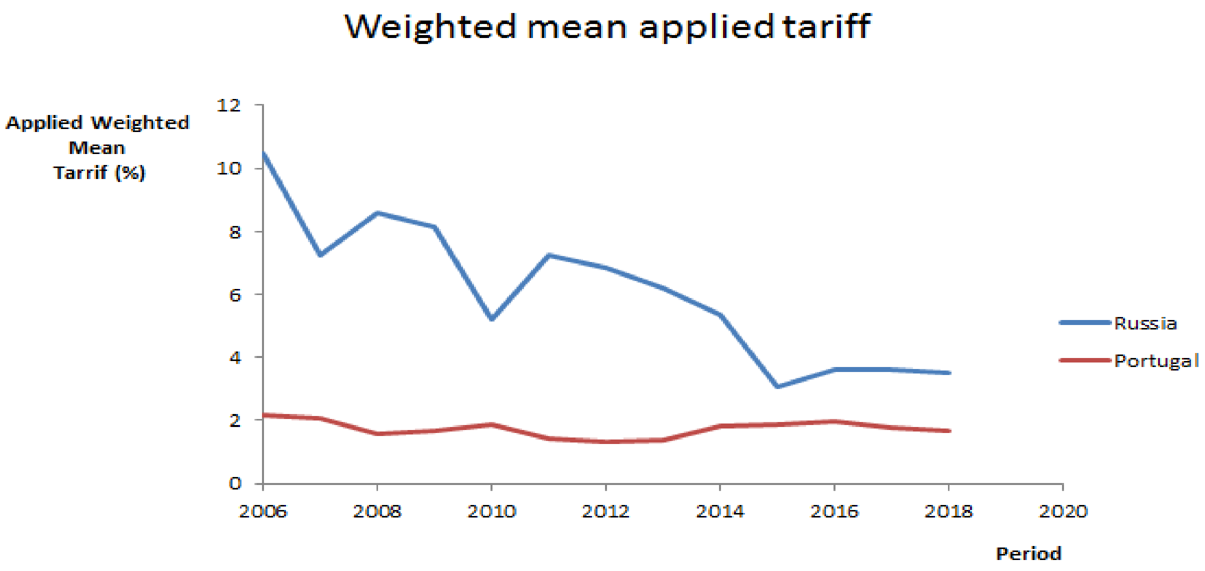

Figure 7: Weighted Mean Applied Tariff based on COMTRADE data (United Nations, 2020)

(The weighted mean average tariff summarizes all the import tariffs applicable for the respective countries. The analysis is based on UN COMTRADE database as at 2020. Historical mean average tariffs are plotted against the respective periods to depict the 15 year trend).

Figure 6 above depicts the average weighted applied tariff for Portugal and Russia. Between 2006 and 2019, Russia's weighted mean applied tariff trend shows an averagely declining trend, while Portugal's mean tariff trend shows a generally constant trend. The average tariff data shows that it is harder to export to Russia than to export to Portugal. Consequently, other factors notwithstanding, Russia exports more to Portugal than Portugal exports to Russia. Therefore, to improve trade relations between the two countries, there is a need to harmonize the tariffs or explore free trade agreements.

4.6 Bilateral Agreements

Investigation of bilateral trade agreements between Russia and Portugal was conducted using two main databases; The Global preferential trade agreements database (The World Bank, 2020) by the World Bank and ICSD Bilateral investment treaties database (ICSID Convention, 2020). Based on the World Bank (2020) database, there is no preferential trade agreement between Russia and Portugal. On the other hand, one bilateral investment treaty was identified from the ICSID Convention database; Russian- Portugal BIT (1994). Arguably, the dismal trade relations between Russia and Portugal can be attributed to the limited number of bilateral agreements.

4.7 Foreign Direct Investment

Figure 7.0 below shows the trend of bilateral foreign direct investment from 2013 to 2019 (Based on available data). Portugal's foreign direct investment in Russia has remained significantly low over the period (Bank of Russia, 2020. Therefore, Portuguese corporations do not consider Russia an important investment target. Similarly, Portugal is not Russia's strategic investment destination. Russia's investment in Portugal covers less than 0.3% of the FDI inflow (UNCTAD, 2020).

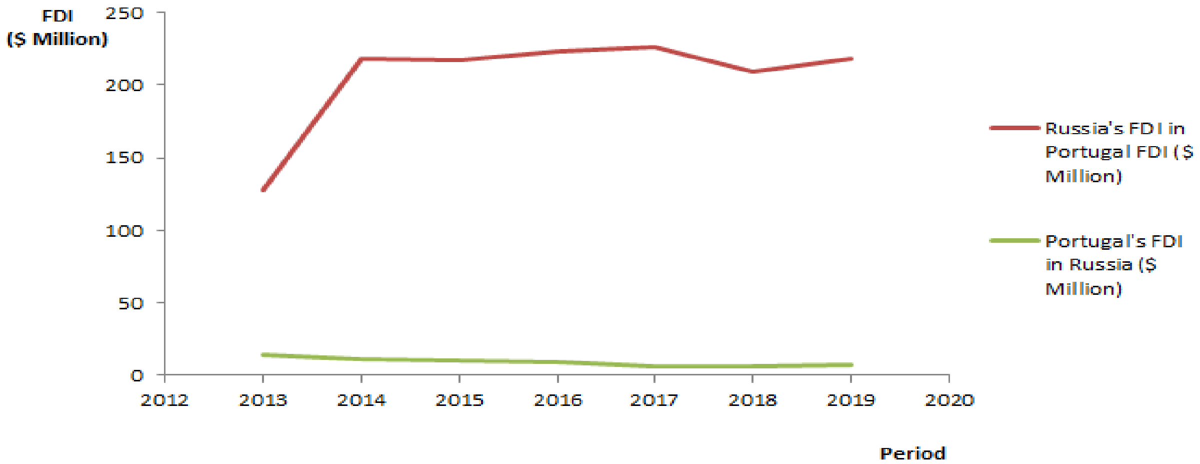

Figure 8: Bilateral Foreign Direct Investment (UNCTAD, 2020; Bank of Russia, 2020**)**

(The foreign direct investment analysis provided in the figure is based on data obtained from UNCTAD and Bank of Russia. The data captures foreign direct investment inflows into Russia and Portugal in USD millions. The figures capture investment both in the private and public sectors)

5. A Study on How to Improve Russia and Portugal Trade Relations

5.1 Discussion

Portugal and Russia are important global trade participants who engage in bilateral import and export international trade activities. According to Shcherbak (2018), Portuguese-Russian relations are mainly characterized by cultural cooperation, trade relations, and economic cooperation. However, existing studies such as Sputnik International (2017) and COMTRADE data (United Nations, 2020) on international trade reveals unfilled international trade opportunities in Russian-Portuguese relations. The study on the improvement of trade relations between Russia and Portugal is a multi-faceted endeavor that can be achieved through different measures. This study identifies three areas of improvement, including trade policies, bilateral agreements, and foreign direct investment.

The history of Portuguese-Russian relations dates back to the 18th century (Nailia, 2017). Based on the trend of value of goods and services traded between Russia and Portugal, the long-standing relationship has not experienced any significant growth in the last fifteen years; trade activities have deteriorated over the period. One of the arguable contributions of the stalled growth can be attributed to the challenges associated with the protectionism embedded in international trade's mercantilism theory. According to Viner (2016), mercantilism theory requires countries to promote exports more than imports. Despite mercantilism theory being a classical theory, it is still prevalent in Russian-Portuguese relations.

Free trade has been identified as one of the effective ways of improving trade relations (Smith, 2010; Williams, 2019). In this study, it is established that Russia is one of the leading economies in protectionism, which has stifled bilateral relations expansion despite the long history of economic cooperation. The protectionist problem on international trade growth has been highlighted in other studies such as Williams (2019) and Cleaver (2019) explored in the literature review. These past studies highlight that protectionism not only limits imports but also inflates the prices of imported goods. Improving trade relations between Russia and Portugal calls for the elimination of trade barriers that hinder international trade.

According to Sputnik International (2017), various opportunities can be exploited to improve Russian-Portuguese relations such as the growing market for luxury goods in Russia, coupled with Portugal's luxury products manufacturing prowess. Other areas include software, tourism, agricultural products, machinery, and tools. The present study's findings support the earlier findings on the existence of trade opportunities between the two countries. For instance, agricultural products, machinery, and tools feature among the top products traded by Russia and Portugal. However, tourism and luxury goods bilateral market opportunities are yet to be exploited. The current trade volumes (2019-2020) between Russia and Portugal are significantly lower than the best-achieved trade volumes in the past 15 years. One possible explanation of the declining trade volumes is arguably the intensifying competition occasioned by preferential trade agreements within the European Union and the Commonwealth of Independent States Free Trade Zone.

Leveraging each country's absolute or comparative advantage, Russia and Portugal can boost the bilateral trade higher values than the existing. For instance, findings on the top products traded between the countries show that Russia has a competitive edge in fossil fuels and constituent products, aquatic products, steel, iron, wood, and agricultural inputs. On the other hand, Portugal has a comparative advantage in agricultural products; Portugal's top exports to Russia constitute agricultural products. Therefore, Portugal and Russia can specialize in various goods in line with the tenets of absolute and comparative advantage theories (Lane and Milesi-Ferretti, 2018; Feenstra, 2015).

Porter’s National Competitive Advantage Theory postulates that a country's competitiveness in international trade depends on the capacity to upgrade and innovate in the concerned industries (Porter, 2011). The findings on the technological advancement index show that Portugal ranks higher than Russia. However, the findings on the country’s competitiveness show that, on average, Russia is more competitive globally than Portugal, though the difference is only marginal. Some of the possible explanations to the mismatch between technological advancement and global competitiveness include other factors highlighted by Porter (2011) as contributors of competitiveness such as natural resources endowment and capabilities, local market demand, and presence of complementary industries. Currently, both countries can be ranked as followers and not leaders in technological innovations. Consequently, Russia and Portugal would inevitably need to seek more technologically, advanced trading partners. Therefore, both countries should focus on continuously improving their technologies and be at the forefront of technological innovations to remain relevant trading partners. Nevertheless, trade relations can be improved through other avenues based on the country's similarity theory (Krugman et al., 2018).

According to Hall (2018), trade policy is one of the avenues identified in the review of existing literature as a key factor in improving trade relations between countries. Fundamentally, trade policies can either act as a barrier or a promoter of international trade. The present study focused on the ease of trading across borders, economic freedom, and tariffs. The findings on the ease of trading show that Russia ranks low to carry out cross-border trade while Portugal ranks first globally. Also, Russia ranks below the world average in economic freedom. The findings agree with Hall (2018), who highlights that restrictive trade policies that impose trade barriers affect how much goods and services a country can import or export. The findings corroborate findings by Pimenov (2018) and The Moscow Times (2014), studies that highlight Russia’s protectionist approach to international trade.

Therefore, the mismatch in economic freedom and ease of carrying out foreign trade between Russia and Portugal requires urgent attention if any trade relations are to be realized.

Another critical component of trade policy encompasses trade tariffs. According to Hall (2018), imposing trade tariffs serves to protect local industries from foreign competition but, on the other hand, acts as an impediment to international trade. The present study's findings highlight that Russia's average weighted mean tariffs are higher than Portugal's. The government's tendency to switch between policies that favor the local firms makes protectionist states unattractive for international trade (Evenett, 2019). Also, it may be beneficial to export to a market with lower tariffs. To improve trade relations, there is a need for preferential trade agreements that would harmonize the tariffs between the two countries to facilitate better trade relations.

Bilateral agreements encompass trade privileges and have been cited as effective tools to eliminate trade barriers between international trade partners (Maluck et al., 2018). A limited number of bilateral agreements exist between Russia and Portugal, the major one being the Russian- Portugal BIT (1994). Partly, the non-existence of preferential trade agreements explains the dismal progress in trading relations between the two countries. To improve trade relations, bilateral trade agreements would go along way in eliminating trade barriers and facilitating more trade inflows and outflows between the countries. Various scholars have highlighted the importance of bilateral relations, such as improving trade volumes, welfare, and GDP (Kohl, 2014; Egger and Larch, 2011; and Zhang et al., 2017). Due to the non-existence of preferential bilateral trade agreements between Russia and Portugal, assessing their bilateral relations impact could not be accomplished.

Finally, boosting foreign direct investments between the countries is necessary to improve trade relations. According to Krugman et al. (2018), foreign trade and foreign direct investment are mutually inclusive and hence no longer a binary choice for partners seeking to deepen trade relations. The existing literature highlights the crucial role of foreign direct investment, such as improving the provision of goods and services, accessing market knowledge, gaining entry into new markets, easier acquisition of inputs, and eliminating trade barriers (OECD, 2020). The present study's findings show that Russia and Portugal are not strategic partners in foreign direct investment characterized by limited and stagnated foreign direct investment in both countries. This finding aligns with an earlier study by Escaith (2017), which highlighted the existing challenges in accumulating foreign direct investment across global value chains.

5.2 Summary of Recommendations

Based on the discussion in the preceding section improvement of trade relations between Russia and Portugal can be achieved through three major recommendations.

1. Development of enabling trade policies that promotes free trade for both imports and exports between Russia and Portugal in order to eliminate the current high tariffs and difficulties in trading across borders.
2. Development of preferential bilateral trade agreements Russia and Portugal. Aspects such as trade barriers and high tariffs can be directly addressed through bilateral agreements.
3. Boost foreign direct investment between Russia and Portugal. Foreign direct investment can help eliminate various costs of trading across borders and hence encourage better trade relations between the nations.

6. Conclusion

Russian-Portuguese trade relations have been in existence for close to two and a half centuries. However, the trade statistics between the two countries reveal mixed results characterized by periods of rising and decline. Various earlier studies have highlighted the opportunities and challenges in Russian-Portuguese trade relations that require addressing. This paper explores how to improve the trade relations between Portugal and Russia informed by existing literature and theories, and empirical evidence gathered from existing secondary data.

Earlier in the study, it was established that Russia and Portugal trade relations are governed by constructive interaction, mutual respect, and partnership. Moreover, various studies and reports highlight the positive nature of the atmosphere surrounding the countries' bilateral relations. To a great extent, international trade is influenced by the political atmosphere governing the ties, hence making it difficult for political rivals to engage in constructive trade relations. Russia and Portugal have enjoyed a long period of peaceful cooperation and are crucial trade partners, hence suitable candidates for this study.

A review of trade statistics and trends between Russia and Portugal reveals the need to improve trade relations. For instance, Russia ranked 42nd in Portugal's export market by dollar value, while Portugal ranked 12th in Russia's export market by dollar value in 2019. Portugal Moreover, various earlier studies highlight the opportunities that can be exploited to boost trade and some of the existing impediments to fruitful trading. However, literature addressing how Russia and Portugal can improve trade relations has not been adequately addressed.

A review of existing literature reveals that bilateral trade relations are mainly centered on imports and exports of goods and services. Different scholars highlight the need for international trade, such as acquire goods and services that would be too expensive to produce locally and need to accumulate wealth. On the other hand, other scholars do not support international trade's perceived benefits, citing the adverse effects on smaller countries, especially exposing them to exploitation by stronger countries at the global markets.

The international trade theories reviewed are broadly classified into classical theories and modern theories of international trade. Besides providing a rationale for international trade, international trade theories represent the development and evolution of the economics of international trade. Despite the progression, modern international trade exhibits traits of different theories. For instance, countries are concerned with the balance of trade even in modern times, a tenet of the mercantile theory of international trade. Another crucial theory is the comparative advantage theory, which encompasses the comparative efficiency of producing different products. Therefore, a country produces commodities it can produce more efficiently than others, and import commodities produced more efficiently in other markets. The most crucial modern theory of international trade identified in this study is Porter’s National Competitive Advantage Theory.

A review of existing literature on the factors that can improve international trade relations between Russia and Portugal revealed three major areas, including trade policies, bilateral agreements premised on preferential trade agreements, and foreign direct investment. Fundamentally, relaxed trade policies are considered catalysts of stronger trade relations, while protectionist policies impede trade relations. The existence of preferential trade agreements promotes international trade while the non-existence of preferential trade agreements impedes trade relations. Finally, foreign direct investment is necessary for deepening trade relations, while limited foreign direct investment impedes the growth of international trade. Other mediating factors that promote trade relations include the level of technological advancement, comparative advantage, and global market competitiveness.

The findings from the review of secondary data and sources provide a picture of the current situation in trade relations between Russia and Portugal and provide a basis for developing a blueprint on how the two countries' relationship can be improved. A historical perspective of the trade relations reveals various findings. Firstly, the countries are operating at sub-optimal levels characterized by slow growth, with several episodes of rising and fall in trade values. Secondly, both countries have unique comparative advantages that can benefit trade relations, i.e., Russia has a comparative advantage in fossil fuel production while Portugal has a comparative advantage in agricultural products and luxury goods. Various mismatches were identified in the level of technology advancement, countries' competitiveness, and trade policies. Only one bilateral agreement was identified coupled with a dismal, almost stagnant trend of foreign direct investment.

Various measures are recommended to improve the trade relations between Russia and Portugal. Firstly, there is a need to harmonize the trade policies governing the bilateral relations between the two countries. Free trade is recommended to eliminate the protectionist trade barriers in Russia. Russia's average tariffs are relatively higher compared to Portugal's, and this needs to be addressed to encourage bilateral trade. Also, the development of bilateral trade agreements characterized by preferential trade terms and enhanced foreign direct investment is recommended to improve trade relations between Portugal and Russia.

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