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NEW ASPECTS OF BELARUSIAN FISCAL POLICY

Nowadays Belarus can be proud of its fiscal achievements, as the budget seems to be balanced. The consolidated general government budget deficit was only 0.6% of the GDP in 2005 and the IMF estimates for this year a 1.5% deficit.

GENERAL ECONOMIC DEVELOPMENTS

Economy of Belarus has been performing very well in recent years. According to IMF data, annual economic growth rate reached 9.3% in 2005 - and a 7% growth rate is estimated for 2006. The most productive sector in Belarus is the service that gives 64% of total GDP, while industry gives around 26% (the rest comes from the agriculture). Besides high growth rates, the inflation rate is also high: in 2005 the prices were in average 10.3% higher than a year earlier and the IMF predicts a 7.9% inflation rate for 2006. However this is in line with the continuous disinflation process.

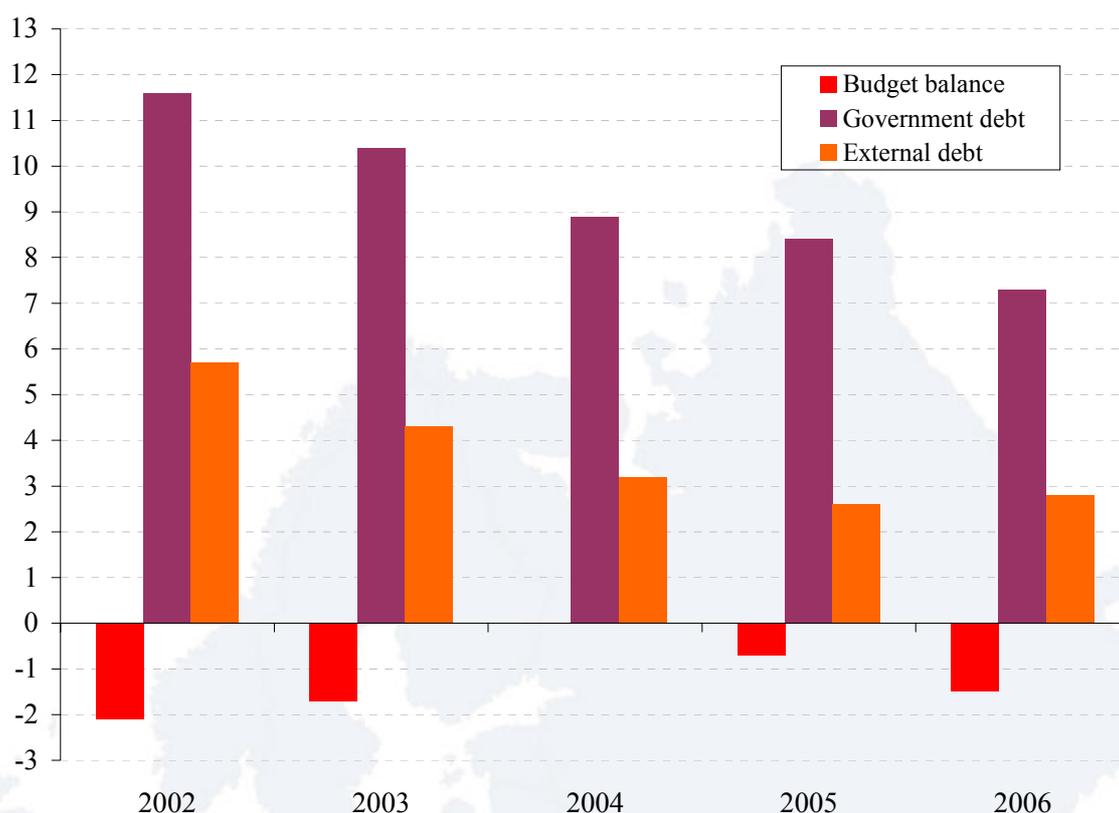
Belarus is a net FDI importer owing to the fact that the country becomes more and more attractive for the foreign investors and the process of privatisation has been started – the cumulated amount of FDI (coming to Belarus) reached the USD 2.3 billion at the end of 2005 (while the foreign direct investment in abroad amounted to only USD 14 million). But this is still very moderate in comparison with comparison of cumulated data of NMS countries.

The trade balance of Belarus has a deficit; the reason for it is mainly that Belarus is a net oil and gas importer. Its main trading partners (both from the side of import and export) are the former CIS-countries, mainly the Russian Federation (more than 47% of the total Belarusian trade turnover is realized through the trade with Russia in the first half of 2006).

Its worth to mention the political structure of the country as it is an autocratic presidential system.

REASONS OF FISCAL STANCE

Beside the budget seems to be balanced; both the government and external debt are continuously decreasing – last year the debt-to-GDP ratio was 8.4% of the GDP and amounted to USD 2.9 billion. The debt consists of mainly long-term loans and trade credits.

Chart 1. Budget Balance and Debt in Belarus (in % of GDP)

Note: data for 2006 is estimation
Source: IMF

It is worth analysing why this good record could be achieved, and what was the main income source of the budget. *Table below* shows that the main sources of the government budget revenue consisted of four different taxes, namely the personal income tax, the profit tax, the value-added tax (VAT) and the excises. These gave 37.34% of the total revenue of the consolidated general government budget in 2005 and it is expected that this rate will increase. The other main source of the revenue is the incomes of the social protection fund – although the total amount of this is less than that of the four main taxes.

Table 1. Rates of the Different Sources of the Government Revenue, 2002-2007

<i>% of total revenue</i>	2002	2003	2004	2005	2006	2007
Personal income tax	6.64	6.10	6.10	6.11	6.79	6.27
Profit tax	5.53	5.57	7.06	7.68	8.68	7.95
VAT	18.61	17.25	16.58	19.12	19.74	19.58
Excises	5.09	4.99	4.88	4.44	7.13	4.73
Property tax	3.35	4.35	4.16	3.73	3.17	4.01
Customs duty	4.50	5.70	4.76	5.46	5.79	5.80
Other	14.19	15.53	15.92	13.00	24.60	13.78
Revenue of budgetary funds	16.43	17.17	17.00	16.45	-	17.06
Social protection fund	25.65	23.34	23.55	24.02	24.11	23.37
Rate of 4 main taxes (%)	35.86	33.91	34.63	37.34	42.33	38.53
TOTAL	100.00	100.00	100.00	100.00	100.00	100.00

Data of 2006 and 2007 are estimations
Source: Own calculation based on IMF data

Why do the taxes play a continuously significant role in the government budget? The main reason is the current reform of the Belarusian taxation system. In 2005 the following reforms were realized in the taxation system:

- Collection of indirect taxes in trade relation with Russia on the basis of the country of origin. This means that tax is imposed on all the import coming from the Russian Federation. This income for the budget is enormous, because more than 60% of the total Belarusian import is from this country
- Taxation of the Belarusian foreign trade with all countries
- Reduction of the rate of turnover taxes (from 4.15% to 3.9%)
- Expanding the taxation base by the reduction of privileges, therefore more private persons and enterprises (who weren't involved in the tax-payers) must pay tax. (But the problem is still the great number of the tax avoiders.)

At the same time, the government is about not to spend more than the available amount of the revenue, and the government tries to reducing the expenditures. The reduction has not been realized so far, but it is expected the annual growth rate of the expenditures will not be higher than that of the revenue. Nowadays the Belarusian government spends the most on social polices (including health – to handle the consequences of Chernobyl or education and social security): the rate of these spheres is more than 50% of the total expenditures. It can be stated that the aim of government is to increase the living standard of the population (according to some analysts it is because of political reasons).

The government doesn't want to finish the reforms and according to economic review of the Ministry of Foreign Affairs of Belarus, the government has determined its fiscal targets for the next period, which lasts from 2006 to 2010. According to these targets, the Belarusian government is about to abolish the small and inefficient taxes between 2006 and 2010, and it tries to realize the development of the administration system, and to reduce the number of tax avoiders. These reforms, leading to a more transparent and simple tax system, are to become a part of the Tax Code of the Republic of Belarus.

On the expenditure side the government plans to implement the principal that all expenditures must be secured by the amount of the budget revenues. Furthermore the government is about to develop the Budget Code of the Republic of Belarus. Beside of these, the main target of the budget policy is not to exceed the deficit level of 1.5% (comparing to the GDP).

These measures (reform of the taxation system, new aspects of the fiscal policy) have enormous affect on the economic growth of the country. If the taxation system becomes more transparent and simple (as it is targeted), on one hand the circumstances of operating for the enterprises will be improved, on the other hand the country will be more attractive for the foreign investors. Both groups of stakeholders are the main generators of the economy, and the target of the more than 8% growth rate of the GDP can be realized in the country in the next few years.

In spite of the good achievement of the Belarusian economy, we have to take into consideration the extensive state intervention. The rate of the revenues compared to the GDP was 48.4% last year (owing to the great number of state-owned enterprises) and this will be largely unchanged this year. The state actions can be high burdens of the plans concerning the future, but the government is about to decrease and to optimise the state-owned property to solve this problem.

TOURISM: AN INCREASINGLY IMPORTANT SECTOR OF ARMENIAN ECONOMY

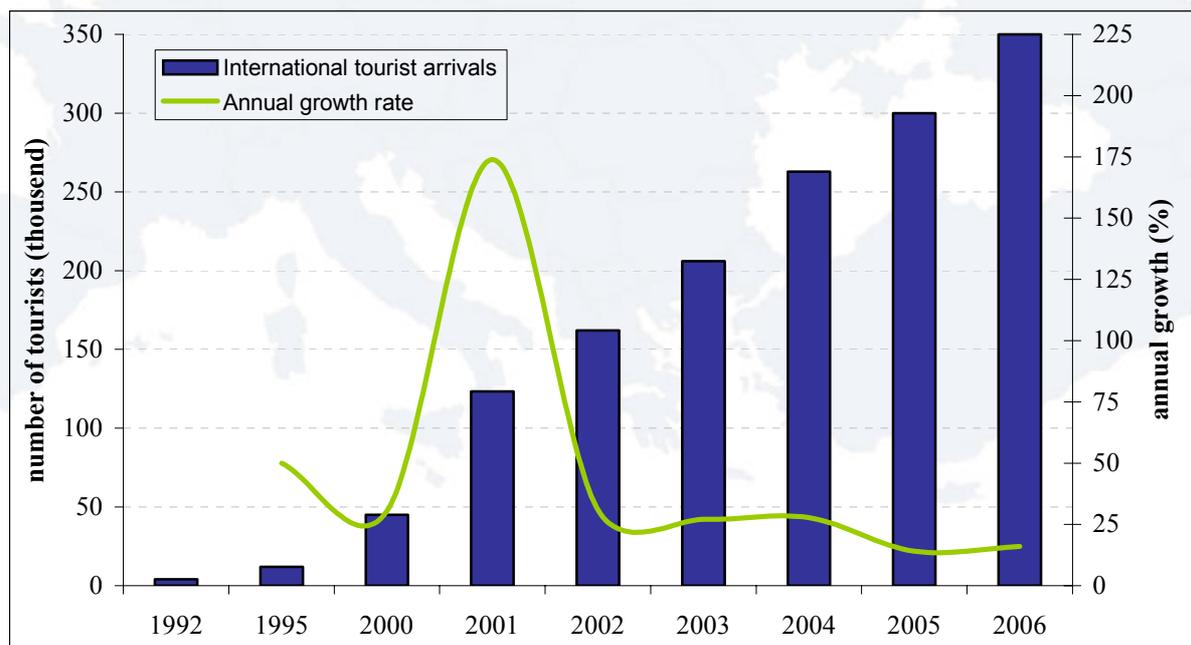
According to the tourism department of the Ministry of Trade and Economic Development, the boom, experienced by the tourism sector of Armenia, has continued in 2006 as well. The number of tourist could reach 350 000 by the end of the year. More optimistic estimations claim that it could approach the 400 000, which would be nearly twice the figure reported in 2003.

TRENDS IN THE ARMENIAN TOURISM

Tourism generates about 7% of the Armenian GDP, thus it became one of the leading industries of the country. In the Soviet years tourism gained already importance, as the number of international tourists reached half a million in 1987, of which only 100 000 were from outside of the Soviet Union. However, the conflict with Azerbaijan over the ethnic, Armenian-dominated region of Nagorno-Karabakh and the break-up of the planned economic system resulted in a severe economic decline in the early nineties. The conflict frightened potential visitors and the number of international tourists decreased to 4-5 thousands in 1992 and 1993.

As tourism is a branch in Armenia that is able to develop even in periods of recession, the recovery of the sector started relatively early. By 1999, the number of tourist arrivals reached 40 000. According to the calculations of the World Tourism Organization, the income from international tourism by one tourist amounts to USD 1 000, thus the export of tourist products and services reached the volume of USD 40 million in 1999. The development was rather slow in the beginning, but became dynamic after 1999, and the average annual growth exceeded 50% between 2000 and 2004. The government set the target of 500 000 visitors by 2010 which seems to be achievable knowing the 2006 forecast of at least 350 000 tourists.

Chart 2. International tourist arrivals and growth rate in Armenia, 1992-2006



Source :National Statistical Service of the Republic of Armenia

Most of the tourists arrived from the EU, having a share of 30.4% in tourist arrivals in the first half of 2006, which is 3 percentage points higher than the figure of the same period of the previous year. 11.2% of foreign tourists arrived from France, and about 5% both from Germany and the United Kingdom. The increase of the number of European tourist arrivals originates from the growth of the number of French tourists. Despite the high proportion of EU tourists, the country giving the most visitors to Armenia, is the United States (22.4% from January to June 2006), followed by Russia (19.8%). The latter show the most dynamic development, as the proportion of Russian tourist grew by 8 percentage points between 2001 and 2006, compared to a 2 percentage-point-growth of the United States. Besides the EU and the United States, CIS countries are the third main region of origin (26.8%).

Two thirds of international tourists are ethnic Armenians, who want to discover their roots. Most of them are second or third generation American Armenians. However, the proportion of Diaspora Armenians is decreasing, and according to the Armenian Tourism Development Agency, much of the anticipated growth will come from tourists not having Armenian roots.

TOURISM DEVELOPMENT STATE PROGRAM 2006-2008

The Armenian government realized that tourism development promotes the development of other economy branches such as transport, communication, trade, construction or production of consuming goods. Thus the sector became a governmental priority and a tourism development initiative was developed for the period of 2001-2003. The initiative aimed to develop the most successful forms of tourism (like cultural and historical tourism, religious tourism, ecotourism, and business tourism) by overcoming hindering factors, such as low quality, under qualified staff, non-competitive prices, the lack of low-cost accommodation, political and economic shocks, and the missing positive image of the country as a tourist destination. Thanks to governmental incentives tourism started to grow faster, but there are still areas that need further improvements.

The Tourism Development State Program 2006-2008 aims to make a more efficient use of the funds directed to the improvement of urban and rural areas favourable for tourism, to improve business environment, to ease the access of the country, to ensure qualified staff and to create an image of Armenia as a country favourable for tourism. According to the program annual revenues from tourism services should reach USD 350-450 million by 2010 and USD 700-900 million by 2020.

The first steps of the program include the definition of 3 or 4 tourism regions, and the establishment of organizing bodies in these zones. Additionally, ruling out of possible obstacles in obtaining entrance visas should be finished by the end of 2006. Other elements of the strategy focus on the improvement of thematic content and quality, the development of infrastructure and accommodation, providing training opportunities for those involved in tourism, limit negative effects of poverty on tourism development and promote Armenia in order to improve its image.

EXPECTATIONS

The Armenian government is committed to develop tourism sector. Based on the implementation of previous tourism development initiatives, it can be concluded that governmental commitment is not limited to writing strategic programs but real action will take place in the period of 2006-2008. As part of promoting the country, Armenian officials will soon launch an advertising campaign on CNN International, BBC and Euronews to show

that Armenia is not a hot spot of conflicts but an interesting travel destination. Implementing the strategy will further boost the tourist sector and also the whole Armenian economy. In order to have more foreign tourists, not only obtaining visas should be eased, but a unilateral visa-free entrance regime should be introduced for citizens coming from developed countries. According to the forecast of the World Tourism Organization the rate of high and stable development (yearly 10%) in world tourism will continue in the coming five years, thus the Armenian objective of 500 000 foreign visitors in 2010 can be considered realistic.



SLOVENIAN PLANS FOR TAX REFORM

After EU accession, objectives of Slovenian government were to cut inflation, meanwhile maintain solid economic growth, decrease unemployment, and to meet the other convergence criteria for Slovenia's entry into the Euro Zone. In line with these goals, the government endeavours to reduce fiscal expenditure as a proportion of GDP and to improve its tax structure after previous reforms.

Further tax reforms are planned to be introduced in order to streamline and simplify the tax system, and distribute tax burden more fairly. The contemplated reforms are elaborated below.

BACKGROUND OF TAX REFORM

The Slovenian economy is one of the most successful countries of transition, as the government managed to establish a stable growth rate, while budget deficit and inflation decreased significantly. As of facts, Slovenian GDP grew by 4.0% in 2005 and the main monetary indicator, inflation rate fell under 3%. Regarding to fiscal discipline, budget deficit has been under 3% of GDP and had amounted to 3.5% in the 1st quarter of 2006 (4.3% in 2005 Q1). The level of unemployment has been declining for years, but still stays above 10 percent (10.2% in 2005). In consequence of prior reforms, the tax system was simplified and modernized, thus the present tax reform aims to maintain the achieved economic stability, but has further goals as well.

As in most of the New Member States, Slovenia displays a high share of indirect taxes (41.5% of total taxes); social contribution plays an important role too with a share of 37.1%. Direct taxes are consequently relatively low, but it must be noted, that employers are also subject to a payroll tax. *Table 2* shows the structure of revenues in Slovenia.

Table 2. Structure of Revenues, 2001-2004

<i>% of GDP</i>	2001	2002	2003	2004
Indirect Taxes (%)	16.1	16.4	16.6	16.5
VAT	8.6	8.9	8.8	8.9
Excise Duties	3.5	3.5	3.5	3.5
Other	4.0	4.0	4.3	4.0
Direct Taxes (%)	7.8	8.0	8.2	8.5
Personal Income Tax	5.9	5.9	5.9	5.9
Corporate Income Tax	1.2	1.5	1.7	2.0
Other	0.6	0.6	0.5	0.6
Social Contributions (%)	15.0	14.8	14.7	14.7
Employers'	5.6	5.6	5.6	5.6
Employees'	8.0	7.9	7.7	7.7
Self- and non-employed	1.3	1.3	1.4	1.4
TOTAL	38.9	39.2	39.5	39.7

Source: Structures of the Taxation Systems in the European Union 2006

A high proportion of indirect taxes are a typical characteristic of transition countries, as it is easier to collect. The structure of taxes according to economic functions is adverse, as taxes on labour are too high and on capital too low. Decreasing tax burden on labour is a strong incentive for improving the level of employment and decreasing the unemployment rate.

Improving competitiveness of companies also come to the fore, as competition in the region is even higher. A composition of taxes according to economic functions is shown in *Table 3*.

Table 3. Taxes According to Economic Functions, 2002-2004

<i>% of GDP</i>	2002	2003	2004
Consumption (%)	14.1	14.1	14.0
Labour (%)	21.5	21.5	21.6
Capital (%)	3.6	3.8	4.2

Source: Structures of the Taxation Systems in the European Union 2006

The tax reform relates mainly to corporate and personal income taxation, but apart from these, the government also adopted smaller changes to other taxes. The contemplated decline in the level of taxes would result a great decrease in government income, so – according to the plans of the government – this shortfall should be offset through lower public spending and higher economic growth.

Until now, the purpose of changes was to decrease inflation, to stabilize economy and to help economic growth. The tax reform aims at reduce the direct tax burden on labour, modernize tax relieves in corporate income tax, spurring investments and improve competitiveness.

PROPOSED TAX REFORM

In September 2006 the Slovenian Government introduced a proposal for changes to corporate taxation and personal income tax (indirect taxes and social contributions are not part of the reform). The direction of the proposal points towards a lower overall tax burden, which means a shortfall in the budget of the government. This shortfall would be compensated with the decrease of public and government spending and higher economic growth. If these were not enough to absorb the contemplated tax reduction, an increase in the measure of VAT rate would be implemented, but no more than 1%.

The reform aims to reduce tax burden on labour (thus treat unemployment) and improve competitiveness of companies.

PROPOSED REFORM TO DECREASE TAX BURDEN ON LABOUR

Personal Income Tax

Personal Income Tax is paid during the year in the form of advance tax payments. The tax rate schedule is fixed and the net amount of income is taxed at progressive rates, specifically the five rates are 16%, 33%, 37%, 41% and 50%. Other forms of personal incomes are taxed according to a flat tax rate. In order to simplify and streamline the tax system and to lower the burden of lower income taxpayers, the following tax rates will be implemented as of 1st of January 2007: 16%, 27% and 41%.

Comparing these proposed tax rates with prior plans of the cabinet, small adjustments were made to the figures. The highest tax rate was planned to be lower and the middle income tax bracket was higher in the first proposal. These changes reduce the possibility of a future increase in VAT rate in order to cover the shortfall from tax reduction, which may be an important message for market players. This would mean by the way a EUR 145.5 million reduction in the revenue from personal income tax, but definitely reduce tax burden on labour.

Direct taxes amounted to 8.5% of GDP from what Personal Income Tax was steady at a level of 6% of GDP.

PROPOSED REFORM TO IMPROVE COMPETITIVENESS

Corporate Income Tax

The corporate tax rate is 25% in Slovenia and there is a reduced tax rate in law, which must not be lower than 10%. This applies to companies conducting their business activity under special conditions, in Special Economic Zones (SEZ). SEZs are areas specified by the Economic Zones Act whereby enterprises operating in these special zones may be granted tax concessions. A special rate of 0% corporate tax also exists.

The corporate tax rate is relatively high in Slovenia comparing to other countries in the region and corporate income tax amounted to a higher share of GDP from year to year, and was 2.9% of GDP in 2005. To improve competitiveness this trend needs to be changed. With lower tax levels, companies have more sources to invest from and thus decrease unemployment indirectly as well in the long-run.

The proposed tax rate shall be gradually lowered according to transitional provisions to 23% in 2007, 22% in 2008, 21% in 2009 and 20% in 2010. Other opinions also exist about the pace of the reduction, which say that the 20% corporate income tax rate should be implemented promptly as of 1st of January 2007, but this would mean a too sharp decline in government revenues.

General investment incentives are also represented by a deduction from the tax base of 10% (20% in 2006 and 2007) of the amount invested in equipment.

FUTURE TAX TRENDS FOR SLOVENIA

In 2005 total tax revenues amounted to 40.8% of GDP, of which fiscal burden contributed with 25.7% and social contributions with 15.1%. There is an on-going growth of fiscal revenues from 2000 but social contributions remained almost at the same level as in previous years.

Table 4. Fiscal Burden Slovenia, 2001-2005

<i>as % of GDP</i>	Taxes	Social Contributions	Total
2001	24.0	15.2	39.2
2002	24.5	15.1	39.6
2003	24.8	15.0	39.8
2004	24.9	15.0	39.9
2005	25.7	15.1	40.8

Source: Ministry of Finance Slovenia

This trend may be turned around with the contemplated tax reform as its purpose is to decrease direct taxes on income. Three direct taxes are related in the reform, of which personal and corporate income taxes will be decreased and the payroll tax will gradually be reduced and completely phased out as of 1st of January 2009. The main goal of the tax reform is to reduce tax burden on labour (thus decrease unemployment) and improve companies' competitiveness through lowering their tax burden as well.

In addition, a more efficient administration of public taxes was aimed for and there is an ongoing discussion on tax reforms that provide for a more neutral distribution of taxes.



OIL AND GAS DOMINATED ECONOMIC STRUCTURES OF CENTRAL ASIA

Despite of the economic-structural problems, countries of Central Asia (Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan) are important players of world energy market, as considerable assets of oil and gas is available in this region. These reserves and their strategic position make this area extremely interesting for world-powers, both in political and in economic terms.

Nevertheless the analysis of only three countries from the region is possible, as there is no available statistics on Tajikistan and Kyrgyzstan, likely because of evanescent role in oil and gas world market. By 2003 Energy Information Administration (EIA) data, these two countries produced the very moderate 400 and 2000 barrels of oil per day.

OIL AND GAS WEALTH AND PRODUCTION

By proved oil reserves only Kazakhstan possesses considerable part (3.3%) of world total by 2005 data, while the shares of Turkmenistan and Uzbekistan are too small to mention. If calculate it in barrels: Turkmenistan 546 thousand, Uzbekistan 594 thousand (as compared with the 39 620 thousand barrels of Kazakhstan). However, production data show more sophisticated view, as Kazakhstan responsible for only 1.6% of world's total, Turkmenistan 0.24% and Uzbekistan 0.14% in 2005. By the length of time that those remaining reserves would last if production is to continue at current level (Reserves/Production Ratio), Kazakhstan's ratio is almost 80 years, Turkmenistan's 8 and Uzbekistan's 13. (*Data source: BP*)

The investigation of gas reserves and production brings more balanced picture. The three countries possess 4.3% of world total with the shares in it: Kazakhstan 1.7%, Turkmenistan 1.6%, and Uzbekistan 1.0%. In gas production Kazakhstan loses its leading position, as it extracts 0.85% of world total in front of 2.13% and 2.02% of Turkmenistan and Uzbekistan, respectively. These data of course lead to worse reserves/production ratios, albeit it seems to be enough for almost 50 and 34 years, respectively. (*Data source: BP*)

As concerns the consumption side of oil and gas demand. Kazakhstan consumes 0.26% of world total oil consumption, Turkmenistan and Uzbekistan 0.13% and 0.2%, respectively. Regarding to gas consumption Uzbekistan is the leader with its 1.6%, followed by the Kazakhstan 0.65% and the Turkmen 0.6%.

OIL AND GAS NET EXPORTS DEVELOPMENT

The economic structures of these countries are very simple that means that they have usually strong monoculture systems based on natural resources or bulk goods of agriculture.

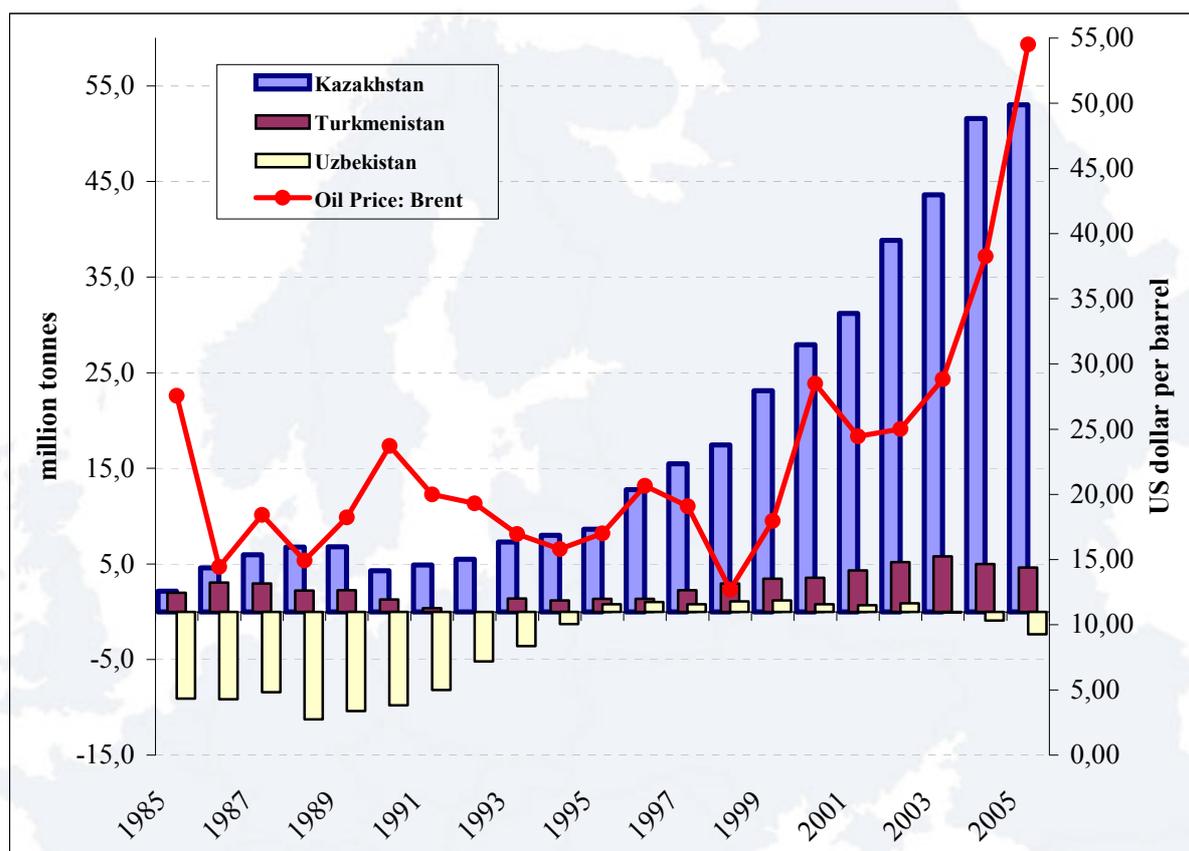
Having a look on development of net exports that is of course in strong correlation with price movements, one can observe different trends in different markets.

Chart 3 below contains data on oil net exports. After collapse of SSSR, Kazakhstan managed to considerably increase its net exports that were due to 13.2% average annual increase of oil production and only 2.3% average annual growth of consumption in the period of 1985-2005. Turkmenistan and Uzbekistan also managed to improve their balances on oil, but in more

moderate peace with fall back in 2004-2005 in Turkmenistan and with deficit in Uzbekistan. During the period 1985-2005, both countries managed to overrun its consumption annual average growth rates by production rates.

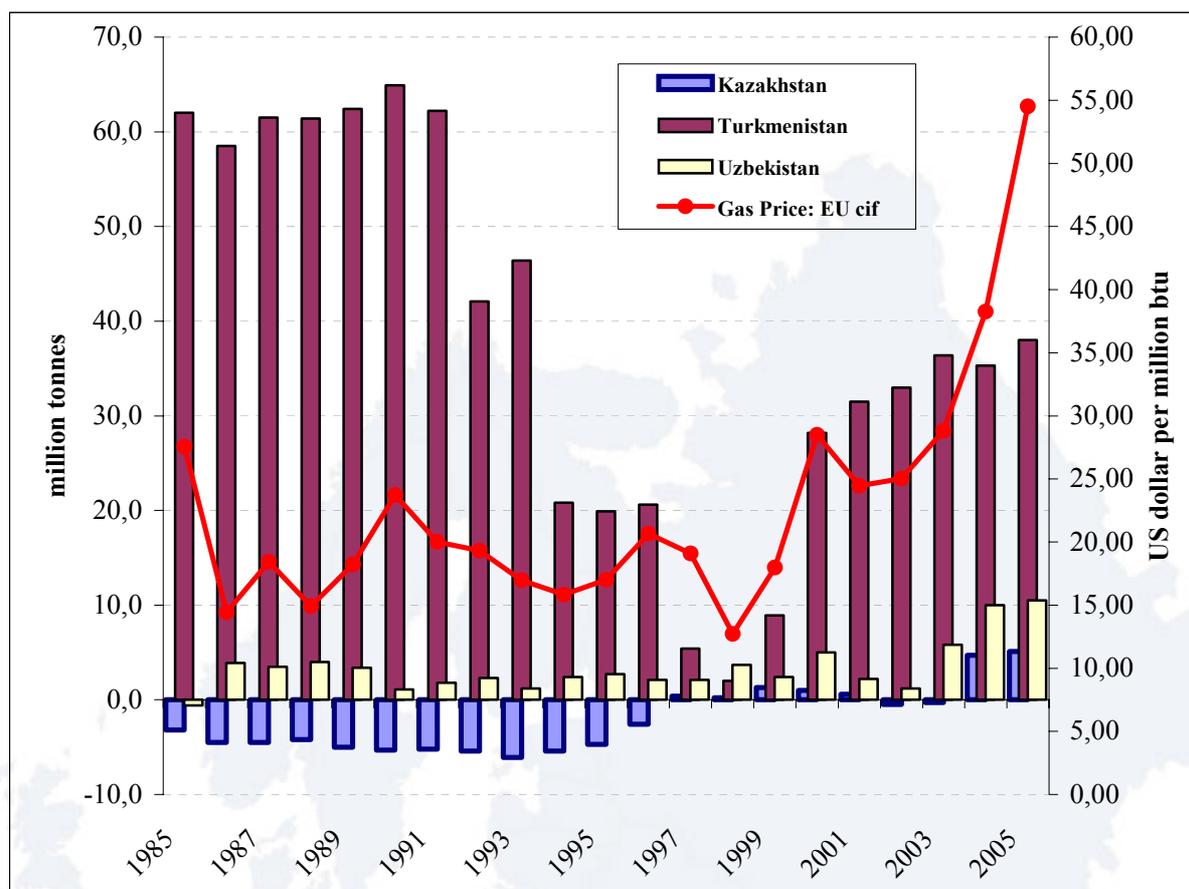
All of these countries experienced considerable slowdown in growth of net exports despite of favourable oil price developments, but in line with transition crisis in their economies. As oil price upward movement made possible to involve more expensive reserves into production, output increased considerably.

Chart 3. Development of Oil Net Exports and of Oil Price, 1985-2005



Source: EIA, BP

Chart 4 that deals with natural gas issue is more likely to show hectic developments. Investigating net exports in the whole period, Turkmenistan is a real “looser”, as it have the balance of almost half of the level observed before the transition, however after financial crisis in Russia and parallel consumed total production, Turkmenistan managed to stabilize its net exports around 30-35 million tonnes. Net exports of Uzbekistan reflect high volatility, mainly driven by fluctuating domestic consumption. Kazakhstan usually consumes all of it natural gas production, only the year 2004-2005 brought remarkable change in this statement.

Chart 4. Development of Natural Gas Net Exports and Gas Price, 1985-2005

Source: EIA, BP

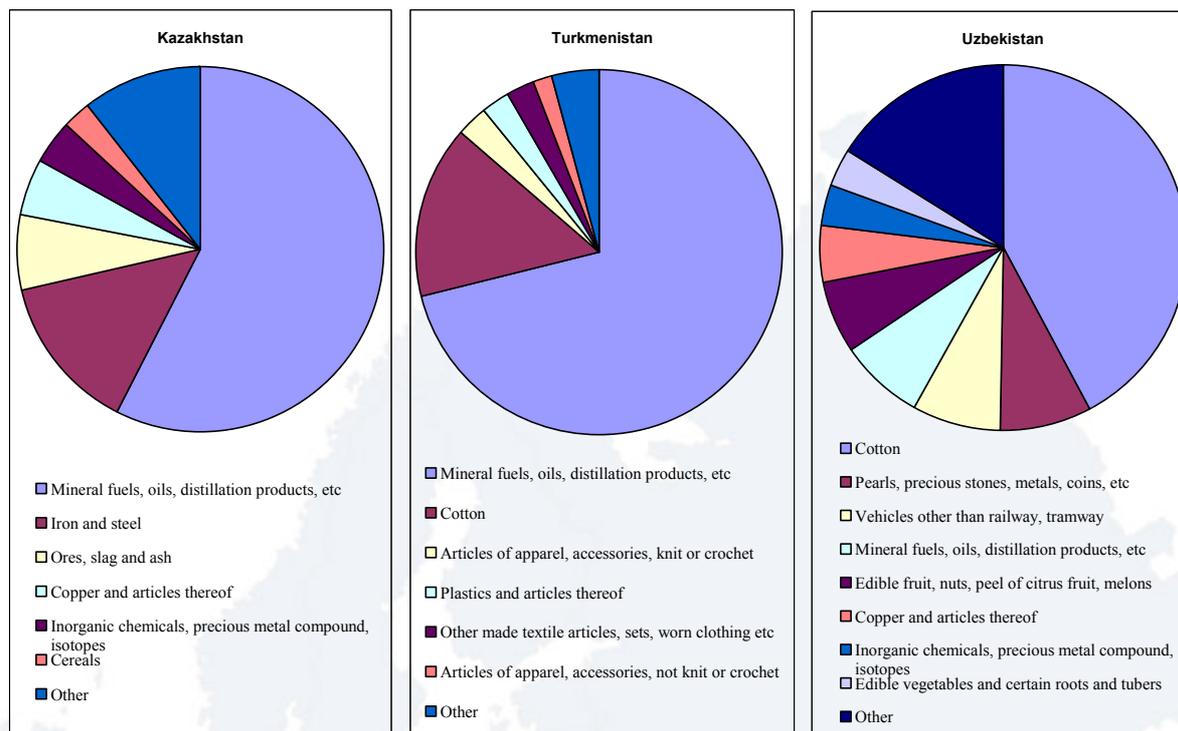
Nevertheless, it is important to mention, that gas production and consumption, thus the net exports depend not only on price developments, but also on available refinery capacities and transportation possibilities (especially pipelines), on changes in demand generated by fluctuations of consumption (particularly in residential consumption influenced by weather), and also by changes in price and availability conditions of substitute energy resources (nuclear, water, electricity, alternative). It is true whereas, prices usually reflect these factors, if there are no considerable interventions from outside the market.

SHARE OF FOSSILS IN EXPORTS

These countries fundamentally rely on exports of few types of goods, usually raw commodities. (See Chart 5) As the export structure is an indicator of development level of an economy, the known statistics raise serious doubts about the future of these countries.

Uzbekistan's distribution of exports by 2004 data shows that 42% of total is cotton, 8% pearls, precious stones, metals, coins, 8% non railway vehicles, 8% mineral fuels, oils, distillation products, 6% of different fruits. This seems quite healthy in comparison with other two countries. Even more biased the export structure of Turkmenistan, as almost 72% of total exports are mineral fuels, oils, distillation products, more than 15% are cotton and its products by 2004 data. Kazakhstan, as the biggest and the most developed country in Central Asia owns the following structure: 58% of total exports are mineral fuels, oils, distillation products, 14% iron and steel (Source: International Trade Centre UNCTAD/WHO)

Chart 5. Export Structure of Kazakhstan, Turkmenistan and Uzbekistan 2004 (as a share of total exports)



Source: International Trade Center, UNCTAD/WTO

CONSEQUENCES

These Central Asian countries are important players of world energy (oil and gas) market. They have a considerable share from oil and gas production if compared with their share of GDP. However, the structure of their economy is heavily relies on those branches that are operating in the oil and gas production and industry. Thus, economic performance depends mainly on world market developments of prices, supply and demand.

The existence of “resource curse” (Ross, M. /1999/: *The political economy of resource curse. World Politics, 51/2, pages 297-322*) is observable in Central Asian development. The reached industrialization level seems to be retrograded. The political situation is stiffened, as these countries autocratic systems. The modernization of entire economy with the help of extra revenues from oil and gas production has failed. Rather the “capital flight” is typical.

The so called “Dutch disease” phenomena also could be a good notion to characterize these countries. Dutch disease is an economic concept that intends to explain a relationship between the exploitation of natural resources and a decline in the manufacturing sector. (Corden W.M. and Neary J.P. /1982/: *Booming Sector and De-industrialisation in a Small Open Economy. The Economic Journal 92, pages 829-831.*) In our case, the development of prices on oil and gas can cause similar processes.