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Relatedness and diversification in EU and ENP countries

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OBJECTIVE

The objective of this working paper is twofold. First, starting from the literature on the role of relatedness between products as a determinant of the diversification process of countries over time, we aim at understanding the differences in this process across different countries, and in particular between countries that are part of the European Union (EU), and countries that are the object of the European Neighborhood Policy (ENP). Second, we also want to study whether other elements beside the past productive structure of countries can have an impact on the direction and speed of diversification process: we focus on the flows of imports and on the productive structure of trade partners.

MAIN RESULTS

The analysis we conduct in this working paper is based on technological proximity, an *ex-post* methodology that uses data on exports flows to infer the relatedness between products. Our results show that both exports

(approximating the productive structure of countries) and imports affect the diversification process into new produces. Moreover, we also observe significant differences between EU and ENP countries. With respect to their own productive structure, ENP countries are characterized by a stronger path dependence than EU countries: this signals that jumping to completely new products is much easier for more advanced countries. With respect to imports, ENP countries are not affected at all, suggesting that at least some capabilities might be required in order to learn to produce new products that are not related to the current productive structure, but are imported in the country. Instead, there are no differences between EU and ENP countries with respect to the role of trade partners: in both cases, trade partners provide only an incentive to keep producing old products and play no role in the diversification process.

These results, although based essentially on theoretical conjectures about the mechanisms, suggest some policy implications. First, policy aimed at improving and speeding up the diversification process should consider that in ENP countries this could be obtained mostly by favoring the development of nearby sectors. Second, policy aimed at improving institutions might help ENP countries to diversify into new products that are more distant exploiting the learning through imports flows.