

This paper investigates the impact of institutions on trade and estimates the potential for trade increase between the Commonwealth of Independent States (CIS) and the European Union (EU). The latter is computed from a gravity equation using the procedure introduced by Hausman and Taylor [1981. Panel Data and Unobservable Individual Effects. *Econometrica* 49 (6) 1377-1398]. We find that CIS trade is still characterized by a large trade diversion effect, which implies that trade with non-CIS countries could increase considerably in the long run. Another source of deepening the level of the European trade integration comes from the convergence of institutions towards the EU standards in light of Russia's application to join the WTO.