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Ukraine in the process of European integration: the economic aspect

Ukraine declared its European integration aspirations for the first time in the Resolution of the Verkhovna Rada of Ukraine from the 2 July 1993 *On the Key Directions of the Foreign Policy of Ukraine*. The document indicated that “the priority of Ukrainian foreign policy is Ukrainian membership in the European Communities, as long as it does not harm its national interests. In order to maintain stable relations with the EU, Ukraine shall conclude an Partnership and Cooperation Agreement, the implementation of which shall become the first step towards its association and, later, full membership in this organization”³.

The political part of the Association Agreement between the European Union (EU) and Ukraine was signed on 21 March 2014. The economic part of the Agreement was signed on 27 June 2014 by Heads of State or Government of the European Union (European Council President Herman Van Rompuy, European Commission President Jose Manuel Barroso) and the President of Ukraine Petro Poroshenko in Brussels. The Association Agreement was ratified by both the Verkhovna Rada of Ukraine and the European Parliament on 16 September 2014.

The Association Agreement is an innovative document and the first agreement based on political association between the EU and any of the Eastern Partnership member countries. Also, this Agreement is unprecedented in terms of its amount (number of spheres that it covers) and depth (commitments and time limits for their implementation in detail).

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³ *Відносини Україна ЄС*, за: <http://mfa.gov.ua/ua/about-ukraine/european-integration/ua-eu-relations> (19.10.2014).

The main part of Agreement is dedicated to key reforms, economic recovery and growth, and also governance and sectoral cooperation in the spheres of energy, transport, environment protection, industry, social development and social protection, equal rights, consumer protection, education, youth and culture.

The Agreement also focuses on the values and principles: democracy and the rule of law, respect for human rights and fundamental freedoms, good governance, market economy and balanced development.

The document provides the strengthening of cooperation in foreign and security policy, including in the energy sector. In addition, issues of justice, freedom and security, and also provision of mobility will be reflected in the Agreement.

The provisions of the Deep and Comprehensive Free Trade Area (DCFTA) that contained in the Agreement go significantly further than classical free trade agreements. They predict mutual opening of markets and stimulation of competitiveness as well and other steps necessary to achieving conformity with EU standards and trade in EU markets⁴.

Accordingly, coming into force of these provisions will significantly impact on the Ukrainian economy, in particular – on foreign trade relations between Ukraine and the EU and with its trading partners, which are not EU members. These are primarily countries of the Customs Union, and first of all it is Russia.

Participation in the process of European integration by the content is not simply international cooperation of economies of Ukraine and the EU, but first of all the process of deep penetration of the EU institutions (legislation, norms and rules of business doing, best practices, etc.) in the Ukrainian economy. In such quality, the EU acts primarily as a factor of influence on internal processes. However, the development of relations with the EU as the global power, an active subject of international economic relations and a member of influential international organizations means that the choice in favour of the EU is also the choice of own place within the world economy in general and in the process of formation and realization of key decisions about global economy development. In this context a crucial role is played by the following factors: the process of trade liberalization, investment flows and labour force migration; convergence of economic regulation norms; participation in programs

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Υπόδα *ηπό* *απορίαση,* za:
http://eeas.europa.eu/delegations/ukraine/eu_ukraine/association_agreement/index_uk.htm (19.10.2014).

of development and activities of integration community's institutions; specific factors of influence over the main sectors of economy⁵.

The domestic economy during 2014 has functioned under the influence of extremely negative external economic factors, which hindered the development of basic economic activities.

Internal risks of Ukraine's economy development are mainly related to:

- military operations in Donbass, which are led to production reduction in the region, deterioration of terms of external financing attraction and growth of budget expenditures to finance War Department and rebuild of destroyed infrastructure;
- increasing of debt burden on the budget because of the need to finance the deficit and debt of NJSC "Naftogaz" that have been formed in previous years;
- International reserves depletion complicates usage by the National Bank of Ukraine (NBU) of interventions as instruments to restrain the increase of demand for foreign currency, which is caused by panic and speculative attacks.

Secondary effects from domestic political and economic shocks, the annexation of the Crimea and the military actions in Donbass have extended on the most sectors of the domestic economy. In a result the existing imbalances are becoming more profound, decline in GDP, reduction the volume of industrial production, of construction works, of foreign trade, reduction the volume of capital investments familiarization, etc. are being accelerated⁶.

At the same time, some kinds of economic activities continue to show relatively high growth rates. Thus, in January-April 2014 the volume of agricultural production substantially increased by 5%, the volume of retail trade turnover increased by 5,6%. The wages increased by 2,3% in January-April 2014 compared to the same period in 2013 (in real calculation).

In the rating of *Doing Business 2014* Ukraine has improved its position by 28 points (up to 112 seat among 189 countries) and has joined the list of 10 countries that improved their performance greatly compared to the previous year⁷.

The further development of trade-economic and investment cooperation with the EU is one of the priorities of foreign economic activity of Ukraine. Prospects for trade and economic cooperation between Ukraine and the EU will increase significantly with the

⁵ Аналітична доповідь, Центру Разумкова, *Європейська інтеграція України: внутрішні чинники і зовнішні впливи*, "Національна безпека і оборона" 2013, No. 4-5 (141-142), p. 27.

⁶ Д. О.Махортих, *Щодо тенденцій розвитку економіки України у 2014–2015 рр.*, за: <http://www.niss.gov.ua/articles/1635/> (12.10.2014).

⁷ Інформація «Про імплементацію Порядку денного асоціації Україна – ЄС у 2014 році», за: http://www.kmu.gov.ua/control/uk/publish/article%3FshowHidden=1&art_id=243281941&cat_id=223345338&ctime=1266423569791 (19.10.2014).

creation of the Deep and Comprehensive Free Trade Area between Ukraine and the EU in the framework of the Association Agreement.

The EU is one of the main trade partners of Ukraine. According to statistical data, the share of the EU in total volume of trade in goods and services of Ukraine in the first quarter of 2014 amounted to 35,37% and increased by 4,4% compared to the same period in 2013.

The foreign trade turnover (excluding the cost of services for alteration of customer's raw materials) in the first quarter of 2014 amounted to 11,46 billion USD (Unites States Dollar), export to the EU-countries amounted to 5,8 billion USD, import to the EU-countries amounted to 5,66 billion USD, active balance amounted to 0,14 billion USD.

International trade balance increased by 1,31 billion USD in the first quarter of 2014 compared to the same period in 2013. The volume of trade in goods in the first quarter of 2014 amounted to 9,95 billion USD, including export – 4,95 billion USD, import – 5 billion USD, passive balance – 0,05 billion USD. The volume of trade in services in the first quarter of 2014 amounted to 1,65 billion USD, including export - 0,99 billion USD, import – 0,66 billion USD, active balance – 0,33 billion USD⁸.

On 12 March 2014 The European Commission submitted to the Council of Ministers and the European Parliament inspections a draft of EU regulation on the application of the autonomous preferential trade regime for the Ukraine, which provides the reduction or elimination of customs duties on goods originating in Ukraine. The parameters of this regime correspond to the provisions of the Ukraine-European Union Association Agreement in the part of Deep and Comprehensive Free Trade Area creation⁹.

23 April 2014 unilaterally the EU has opened its market for Ukraine. And all the trade preferences provided for by the Association Agreement, unilaterally, have been practically applied. Therefore, the EU has set rates of import duty and tariff quota for Ukrainian products at a level that will act in the first year after the introduction of a free trade area between Ukraine and the EU. The autonomous trade preferences (ATP) will be applied until 1 November 2014 and later they must be replaced by the provisions on the Free Trade Area (FTA)¹⁰.

Article 4 of the Association Agreement which establishes a Deep and Comprehensive Free Trade Area is planned to enter into force on 31 December 2015.

⁸ Інформація «Про імплементацію Порядку денного асоціації Україна – ЄС у 2014 році», *op. cit.*

⁹ Торговельно-економічне співробітництво України та ЄС, за: <http://mfa.gov.ua/ua/about-ukraine/european-integration/ukraine-eu-trade> (11.10.2014).

¹⁰ Інформація «Про імплементацію Порядку денного асоціації Україна – ЄС у 2014 році», *op. cit.*

The norms and principles of DCFTA Ukraine-EU provide liberalization of trade in both goods and services, liberalization of the flow of capital and to some extent – the labour force flow. The distinctive feature of the Ukraine-EU FTA is a comprehensive adaptation program of regulation norms in sectors connected with trade to the relevant EU standards. This will allow to mostly eliminate non-tariff (technical) barriers to trade between Ukraine and the EU and to provide the enhanced access to the EU internal market for Ukrainian exporters and simultaneously European exporters to the Ukrainian market.

Thus, the implementation by Ukraine of the Association Agreement between Ukraine and the EU principles in the part of a DCFTA will allow to significantly expand access of Ukrainian exporters to the EU market, removing non-tariff trade barriers in the form of different standards and requirements, will assist to improve the business and investment climate in our country on the base of EU norms and standards, will be an effective mechanism for the gradual integration of Ukraine into the EU internal market.

Deep and Comprehensive Free Trade Area is a part of the Association Agreement between Ukraine and the European Union and one of the most ambitious bilateral agreements concluded by the EU.

Ukraine DCFTA will provide possibilities for Ukraine to upgrade its trade relations and economic development. The instruments for this are: the opening of markets through the gradual abolition of customs tariffs, providing duty-free access within the quota, and large-scale harmonization of Ukrainian legislation, norms and standards with those which act in the EU in various sectors directly or indirectly connected to the trade. This will create the conditions for Ukraine and the EU standards harmonization in key areas.

The final document of a Deep and Comprehensive Free Trade Area consists of 15 Chapters, 25 annexes and 2 protocols¹¹.

The major achievements of Agreement can be generally identified, as following¹²:

1) the improvement of conditions of exports of Ukrainian products to the EU primarily due to the elimination of import duty and reduction of non-tariff barriers to trade in agricultural products.

In recent years, the share of the EU market comprises on average 33% of total exports of goods in Ukraine. The share of imports from EU countries-members was on average 35,6%. Thus the EU market has a significantly higher tariff protection, primarily for agricultural goods and products [current average arithmetic rate of importable duty in the

¹¹ *Торговельно-економічне співробітництво України та ЄС, op. cit.*

¹² *Угода про асоціацію, op. cit.*

EU only on customs tariff is 7,6%, Ukraine – 5,0%, and for goods of groups Nomenclature 01-24 (agriculture) – 19,8% and 9,2% respectively. Meanwhile, rates of import duty from the EU side for individual tariff lines are 1,5-14 times higher than rates of import duty of Ukraine].

The establishment of a Free Trade Area will provide additional benefits to domestic exporters in the market with high sufficiently protection. According to the reached agreements the liberalization covers more than 97% of tariff lines (or more than 95% of bilateral trade between the Parties). Thus, the abolishment of EU import duty on most goods will take place during the first year of the enforcement of the agreement (with 99% of tariff lines).

Besides, the Ukrainian exporters will have an additional advantage for goods on which the EU offered to introduce tariff quotas. First of all it is about pork, chicken, sugar, etc. These products are sensitive to the EU and are usually excluded from the FTAs and are covered by the general customs tax regime. However, as a result of negotiations Ukraine got the opportunity to export to EU the fixed volumes of above mentioned goods under zero import duties. This is not about restriction of imports, but it means only that the import of these goods that will be above the fixed volumes falls within the scope of the general import regime applied to Ukraine today.

The specified above will facilitate the growth of exports of goods and services (exports of agricultural products and food products, including confectionery may increase most notably in particular – exports of textile and leather industry, metallurgy and metal processing, chemical manufacturing, transportation services and services for legal entities).

Meanwhile, a slight increase in imports of goods and services will be observed (the largest increase is being expected in imports of chemical products and machinery; significant growth – in food production and agriculture, production of non-metallic mineral products, textile and leather industry, other types of manufacturing, transport and financial mediation).

According to the World Bank preliminary estimates based on General Equilibrium Model, an establishment of Free Trade Area with the EU, compared with presently existing high tariff protection of EU agriculture could significantly expand production of the agricultural sector in Ukraine and render Ukrainian exports with a general economic effect of 200 million USD per year, or 0,4% of the GDP.

2) acceleration of economic growth. The additional growth is expected mainly due to economic activities such as agriculture and food processing, textile and leather industry, metallurgy and metal processing, transportation services, services for legal entities;

3) increase in the number of employees in economic activity: the growth relative to baseline is expected mainly due to economic activities such as agriculture and food industry, trade and repair, transportation. Meanwhile the slight decrease in the number of employees in the chemical industry, production of machinery and equipment is expected;

4) expansion of the state budget revenues. Taking into consideration the international experience of FTA functioning, short-term loss of revenue due to tariff liberalization will be offset by an increase in other items of revenue by means of domestic taxes;

5) encouragement of foreign direct investments in Ukraine: the establishment of “FTA+” with the EU will become a powerful additional argument in favour of foreign direct investment in the production of goods or services targeted on export to the EU countries using the existing competitive advantages of the Ukrainian economy;

6) improving the business and investment climate for domestic business operators: the process of legal adaptation of “FTA+” and enhancing the quality of its implementation will result in improvement of the business environment in Ukraine in general;

7) benefits for the Ukrainian consumers: the gradual elimination of existing tariff and regulatory barriers to increase the variety and quality of products and services available to consumers. In addition, competitive pressures, stemming from liberalization of market access, encourage specialization, thus stimulating innovation and reducing costs of production;

8) the EU rejection to use export subsidies in trade with Ukraine¹³.

Thus, the plan of economic reforms that should be realized in Ukraine has to proceed from EU integration aims, to foresee comprehensive preparation of Ukrainian economy, society and the state for the implementation of the Association Agreement with the EU.

Real economy reforming should be oriented on a comprehensive modernization that includes:

- development of production capacities for deep processing and producing of high quality final products;
- gradual decrease of share of obsolete resource-intensive low-tech productions;
- reduction of energy intensity on the base of widespread introduction of energy efficient technologies and usage of potential of renewable energy sources;
- gradual harmonization of national production standards with EU standards.

¹³*Provisions of Association agreement between Ukraine and the European Union on free trade area, za: http://me.kmu.gov.ua/control/publish/article/main?art_id=202330&cat_id=202329 (11.10.2014).*

The main lever for achieving the modernization aims is creation of favourable business and investment climate in the country. For this aim it is necessary in top-priority order:

- to implement a comprehensive state policy stimulating the development of entrepreneurship in the country that has to concentrate and coordinate the efforts of all key ministries under the authority of Cabinet of Ministers of Ukraine;

- to simplify the administration of taxes and charges, and customs duties, by the way of bringing them into a unified system of accounting, in accordance with the common standards in the EU-countries;

- to start the formation of a clear and transparent system of government support of economic entities, harmonized with World Trade Organization (WTO) norms and regulations of the European Union;

- to improve the procedures of technical regulations, standardization and certification on the base of preparation for the introduction of EU technical regulations, to ensure the formation of inter-state mechanism of Nostrification of national technical requirements in the markets of the EU member-states;

- to form effective mechanisms to protect the property rights of entrepreneurs and investors;

- to stimulate the competition in the domestic market through more active counteraction to monopolistic practices;

- to improve the mechanisms and instruments of budget and tax policy and monetary and credit policy, taking into consideration Europe's best practices – to direct them to expand the investment potential and activation of enterprises investment activity;

- to increase the effectiveness of public investment by the way of concentration of investment resources on the identified priority areas;

- to increase cardinally the control over the spending of budget means directed at investment purposes, to intensify the practice of public-private partnerships;

- to accelerate formation of institutional surroundings for innovative development, to stimulate commercialization and to provide introduction of innovations in production processes, to ensure the development of new organizational and legal forms of innovation activities, in particular a cluster model of organization of industrial production;

- to establish effective mechanisms for implementing the system policy of domestic trade development, infrastructure of bringing goods from producer to consumer;

- to increase cardinally the level of transparency of public procurement system, to adjust it to the typical international requirements, to foresee anti-corruption mechanisms in

the process of public procurement, to improve the access of subjects of small and medium enterprises to public procurement procedures;

- to form a standing system of control over the quality and safety of domestic and imported products with the norms of the EU, to enhance the control of products quality selling in the domestic market;

- to start the formation of the system of export support of Ukrainian economic operators, which will include the spread of export crediting, insurance, information and legal support of exporters, allocation of assistance for small and medium businesses to expand to foreign markets.

The modernization of system of social protection and labour force market in the context of European integration processes has to anticipate:

- reorientation of higher education and rebuilding the system of vocational training, including on the basis of public-private partnerships with the aim of approaching the qualification structure of employees to the needs of the reformed economy;

- drastic strengthening of target mechanisms and preventing inappropriate usage of social care means;

- further developing of implementation of insurance principles of protection from unfavourable life events (unemployment, full, partial or temporary disability, loss of breadwinner, etc.);

- completion of complex of measures as to introducing accumulative and professional pension insurance;

- health care reform with accent on the implementation of effective mechanisms of organization of quality and affordable for every citizen health service, prevention of the spread of disease incidence and practice of healthy lifestyle;

- special attention to public housing policy, with the creation of effective mechanisms of real softening of housing provision problem mostly on credit basis.

Strengthening of environmental responsibility of the government, businesses and society will assist to adoption by Verkhovna Rada of Ukraine the Strategy of Sustainable Development, harmonized with EU documents. It is appropriate to pass National Conception of implementation and development of eco-friendly production in Ukraine. It is necessary to proceed the work with the harmonization of legislation of Ukraine with the requirements of EU law in environmental protection and implementation of European environmental standards. Ukraine will adhere to obligations to donor countries on the construction of the

New Safe Confinement «Shelter» at the Chernobyl nuclear power plant will carry out the modernization of power units of nuclear power stations together with the EU¹⁴.

The integration of Ukraine into the EU will provide its entry to the world's most powerful regional association, which significantly affects the overall dynamics, structural changes, the level of technology and the format of the regulation of the global economy.

Ukraine unconditionally shares the basic principles of the European Union which are pointed out in the Copenhagen criteria of EU in particular democracy, respect for human rights and fundamental freedoms, rule of law, competitive market economy. Ukraine maintains European policy of Eastern Partnership and expects for the support from European Union and the member-states of EU. The way of Ukraine to the European Union determines fundamental principles of foreign and internal policy of Ukraine.

Streszczenie

Artykuł analizuje aktualne trendy, problemy i perspektywy rozwoju Ukrainy w zakresie europejskich procesów integracyjnych. Szczególną uwagę przywiązuje się do integracji europejskiej w sferze gospodarczej. Artykuł odnosi się również do podstawowych wskaźników rozwoju gospodarczego Ukrainy. Autorzy zauważają, że podstawowe cele polityki zagranicznej i wewnętrznej Ukrainy są determinowane przez jej drogę do Unii Europejskiej. Integracja z UE pozwoliłaby Ukrainie na wejście do struktury o wyjątkowym znaczeniu w regionie, co znacząco wpłynęłoby na ogólną dynamikę tego państwa, zmiany strukturalne, poziom technologii i kształt współpracy z zakresu gospodarki światowej.

Słowa kluczowe:

gospodarka krajowa, rozwój ekonomiczny, proces integracji europejskiej, reform, Ukraina, Unia Europejska

Key words:

domestic economy, economy development, the process of European integration, reforms, Ukraine, the European Union.

¹⁴ *Європейський порядок денний для України – 2014, за: http://www.niss.gov.ua/public/File/2013_nauk_an_rozrobku/Evropskyj%20poryadok%20dennyj%202014.pdf (12.10.2014).*

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