

**Macroeconomics**

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**ASSOCIATION AGREEMENT  
BETWEEN UKRAINE AND EU:  
LONG-TERM OPPORTUNITIES  
FOR COOPERATION AND RISKS  
OF FREE TRADE AREA (FTA/DCFTA) +**

**Abstract**

The consequences of the implementation of the Association Agreement between Ukraine and the EU were outlined. The main of them were the participation of Ukraine in the FTA+ as a unique model of intensive access to European markets, the prospect of attracting foreign investment into the Ukrainian economy, achieving positive effects of reforms. The basic parameters of the Agreement as the potential for cooperation in trade, comprehensive regulation of the international movement of production factors, mutual solution of economic, social and environmental interests of the EU and Ukraine were determined. FTA+ risks for certain sectors of domestic economy were analyzed and ways to minimize them, priority allocation of state efforts to strengthen the competitive position of the main types of goods and services were outlined.

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**Key words:**

The Agreement, FTA, import duties, association, trade regime, tariff barriers, cooperation, competitive position, macroeconomic effects.

**JEL:** F10, F15, F18.

**Introduction.** The current development of the global economy is characterized by the growing number of trade agreements with a focus on mutually coordinated strategic goals and directions, increasing their complex nature. For developing countries, agreements on economic cooperation with the higher level of social and economic development is extremely important, as it enables not only increase the welfare of the country by reducing barriers to the international movement of factors of production, but to adapt to more effective regional model of socio-economic development in general (Filipenko). The Association Agreement between Ukraine and the EU in its content belongs to a new generation of regional trade agreements of 21<sup>st</sup> century. It is the most ambitious agreement which ever concluded in the framework of the EU Eastern Partnership means the DCFTA format, which involves priority allocation of effort on deep and comprehensive free trade area (DCFTA).

**Purpose of the article** – the study of opportunities and risks for Ukraine, the influence of a deep and comprehensive free trade on the Ukrainian economy.

**Tasks of the article** are to highlight the priorities of the trade agreement on the criteria of the dominant direction of Ukraine – EU Cooperation, cumulative economic effects of different sectors of the economy.

**Analysis of recent research and publications.** Problems of free trade zones have been investigated and substantiated by Ukrainian scientists, including O. Shnyrkov who investigated the possible effects of the FTA on the territory of Ukraine and suggested ways of entering the commercial space of the EU; A. Filipenko who opened priorities of FTAs Ukraine; A. Amosha who analyzed the information provision process of forming free trade areas; FTA modes of reflection were observed in publications of V. Lyashenko; FTA regulatory process were described in studies of Yu. Makogon, V. Kravchenko; problems and solutions in the area of free trade were raised in studies of N. Osadcha.

Ukraine access to the European market in the form of DCFTA and economic effects of this unique model of international cooperation were investigated by Ukrainian scientists, such as V. Geyets, V. Grechyn, T. Ostashko, A. Filipenko, L. Shynkaruk and others. However, there is necessity to study Ukraine's transition to more complex forms of trade cooperation with the EU in the framework of the DCFTA.

**Research results.** In a general sense, FTA is a type of international integration, in which participating countries abolished customs duties and quantitative restrictions in mutual trade. DCFTA between Ukraine and the EU provides for the abolition (in some cases a significant decrease) of export and import duties Ukraine approximately 97% of the EU – 96,3%; import duties on industrial goods Ukraine by 82,6%, the EU – by 91,8%; agricultural products for Ukraine abolished duties on 35,2% of tariff lines in the EU – by 83,1%.

For 52% of tariff lines Ukraine introduces a transitional period lasting from 1 to 7 years, to 9,8% – a partial liberalization to 3% – duty-free tariff quota. It means that for particularly sensitive sectors DCFTA Ukrainian manufacturers need more time to adapt to the competitive environment. Thus, due to cancellation fees Ukrainian exporters will save 487 million euros annually and the EU – 391 million (Hayliyer and Piatnytsky, 2013, p. 18).

In the table 1 there is detailed information about a change of customs duties as a result of the introduction of the FTA+ for major export commodities from Ukraine, which account for almost 60% of total exports to the EU.

Table 1

**Changing Ukraine customs duties  
in trade with the EU according to the Association Agreement\***

(prepared by the author that is based on:  
Hayliyer and Piatnytsky, 2013, pp. 11–12)

Goods	EU Duty that Ukraine pays now	Duty / quota for FTA +
<i>Exports of agricultural products in the EU</i>		
Vegetables, fruits and nuts (HS 0713, 0802, 0811)	Up to 20,8%+8,4€ /100kg/net	0%
Wheat (HS 1001)	Up to 186 € / t	0% for the first 950 thousand tons with an increase up to 1 million tons in 5 years. Exports in 2012 – 1,522 million tons

Goods	EU Duty that Ukraine pays now	Duty / quota for FTA +
Maize (HS 1005)	Up to 94 € / t	0% for the first 400 thousand tons with an increase up to 650 thousand tons in 5 years. Exports in 2012 – 1,182 million tons
Soy beans, seeds and oil seeds (HS 1201, 1204, 1205, 1206, 1207, 1507, 1512, 2306)	Up to 9,6%	0%
Chocolate products (HS 1806)	Up to 43%	0% for the first 2 thousand tons with an increase up to 3 thousand tons in 5 years Exports in 2012 – 45 thousand tons
Fruit juice (HS 2009)	Up to 33,6%+20,6 €/100 kg/net	0% for the first 10 thousand tons with an increase up to 20 thousand tons in 5 years. Exports in 2012 – 42,56 thousand tons
Alcohol (HS 2208)	Up to 1% vol/hcl+6,4 €/hl	0% for the first 27 thousand tons with an increase up to 100 thousand tons in 5 years. Exports in 2012 – 11 thousand tons
<i>Exports of non-agricultural products in the EU</i>		
Mineral fuels (HS 25-27)	Up to 2,6 € /t/net	0% transition up to 3 years
Chemicals (HS 28-38)	Up to 17,3%	0% transition up to 7 years
Plastic products (HS 3907, 3920, 3923)	Up to 6,5%	0% transition up to 3 years
Wood and wood products (HS 4401-3, 4407, 4410, 4412, 4415, 4418)	Up to 10%	0% transition up to 5 years
Textiles and clothing (HS 5601, 6303, 6307)	Up to 12%	0%
Equipment and Electronics (HS 84-85)	Up to 14%	0% transition up to 7 years
Vehicles and machinery (HS 8606, 8708, 8802, 8901)	Up to 7,7%	0%

Goods	EU Duty that Ukraine pays now	Duty / quota for FTA +
Medical Equipment (HS 9018, 9401, 9403)	Up to 5,6%	0%
Sports Equipment (HS 9506)	Up to 4,7%	0%

\*According to the calculations based on the authors' analysis of tariffs and tariff quotas for the main 100 products exports in 2012, accounting for 60% of total exports.

The harmonization of technical standards parties minimizes non-tariff barriers, will improve product quality in the domestic market. It will promote a positive image of Ukraine in the world markets as a manufacturer of quality goods, and eventually all of which can lead to increased production.

Studies of CEPS, IFW & ICPS (2006), ECORYS (2008) allowed to determine the number of sectors in Ukraine, in which there is the ability to increase production due to harmonization with EU rules and regulations (see table 2).

Table 2

**Prediction increase of production in Ukraine\***

(Hayliyer and Piatnytsky, 2013, p. 13)

	The amount of production in Ukraine
Agriculture, fishing and forestry	+1,1%
Cereals / oil seeds	+1,1%
Meat	+2,2%
Sugar / confectionery	+4,7%
Vegetable and animal oils	+5,5%
Fruit and nuts	+3,8%
Equipment and Electronics	+7,4%
Cars / spare parts	+4,7%
Transport equipment	+3,3%
Ferrous metals	+2,6%
Metal products	+5,8%

\*Prediction was done on the base of CEPS, IFW & ICPS (2006) researches: Prospects for Deep Free Trade Agreement between the EU and Ukraine and ECORYS (2008): Assessing the impact of DCFTA between the EU and Ukraine.

Modification of competitive relations that result from the trading community of Ukraine – EU will contribute to strengthening positive economic effects; will provide the state transition from periodic to the coordinated participation in European trade space.

According to ECORYS (2008) and the Institute of Economic Research and Policy Consulting of the German Consulting Group (2011) in the long-term the FTA+ between Ukraine and the EU will increase Ukraine's GDP by 0,5% annually, and generally welfare of citizens by 1,2% per year. Concerning the economic indicators, the volume of exports to the EU should increase by about 6, 3%, the volume of import – by 5, 8%, and the average salary – by 5,5% ((Hayliyer and Piatnytsky, 2013, p. 3). In addition, FTA+ covers a wide range of complex issues related to trade, starting from the market access, technical regulations, sanitary and phytosanitary measures, ending with the matters of competition policy, simplifying customs procedures, movement of capital.

Liberalization of access to EU markets will push for redistribution segments of the national economy in the context of the formation of competencies and resources for economic growth enhance partner interactions on the respective trading platforms of European Union member countries. The question of the correlation of different growth factors that, taken together, reflect economic effects in the context of the benefits of trade liberalization and the perceived risks is not observed yet (see table 3).

Table 3

**FTA + impact assessment for major industries of Ukraine**

Advantages	Caution
<i>Siderurgy</i>	
1. Abolition of customs duties should cause a 0,4% increase in output of metal products in the short term. 2. Increasing of export proceeds for 25–30 million euros. 3. Avoiding of anti-dumping duties. 4. Increasing of export proceeds for the pipes for 30 million euros.	1. Cost increasing of reducing the harmful environmental impact. 2. Complete closure of steel market of the Customs Union for Ukraine that will lead to over production in Ukraine within 3,6 million tons of production. 3. Reduction of steel production in the medium term to 0,2%.
<i>Machine building</i>	
1. Acceleration of modernization on the basis of scientific and technological achievements of the EU	1. Increasing in the domestic market of Ukraine competing import of cars, tractors, combine harvesters.

Advantages	Caution
<p>(30% of new technologies).</p> <ol style="list-style-type: none"> <li>2. Adaptation to technological, health and environmental standards of the EU.</li> <li>3. Setting of the basic import duty rates for types of investment engineering products.</li> <li>4. Reduction of import duty on vehicles by 30%.</li> </ol>	<ol style="list-style-type: none"> <li>2. High barriers to entry of Ukrainian manufacturers on the European market because of low technological level.</li> <li>3. Will increase the dependence on imports of domestic engineering high-tech products.</li> <li>4. Will increase the demand for innovative high-tech kinds of imported machinery products.</li> </ol>
<i>Wood industry</i>	
<ol style="list-style-type: none"> <li>1. Ukraine has great potential exports of wood.</li> <li>2. Will increase the prospects for economic cooperation between Ukraine and the EU to expand foreign market wood-products manufacturing.</li> </ol>	<ol style="list-style-type: none"> <li>1. There is a possibility of import growth of products with high added value.</li> <li>2. Will increase the trend of increasing commodity exports.</li> </ol>
<i>Energetics</i>	
<ol style="list-style-type: none"> <li>1. The agreement establishes the commitment made earlier in the European Energy Community and establishes clear timetable of their implementation since the entry into force of the agreement.</li> <li>2. Objectivity of reform implementation.</li> <li>3. Stabilization of power supply of Ukraine's economy and energy sector integration to continental energy markets following the implementation of reforms and their adequate financial support.</li> <li>4. Intensifying the investment process up to 2020 will promote the competitive advantages of Ukrainian products in the long term.</li> </ol>	<ol style="list-style-type: none"> <li>1. Total expenses to achieve energy efficiency up to 2020 may be 86,0 billion euros.</li> <li>2. Total expenditure on infrastructure for 2020 should be 100,7 billion euros.</li> <li>3. In the industrial sector capital intensity will increase by 30%.</li> <li>4. There will be increase in the average cost of electricity</li> </ol>

\* Prepared by the author based on (Heyets et al.,2014, p.102)

According to the author, the following areas should be provided to reduce risks FTA + with the EU for Ukraine's economy:

- promotion of businesses to technological renovation and modernization of production processes in order to avoid major imbalances technological structure;
- enhancing of geographical diversification of exports;
- stimulating of national economy investment support;
- implementation of the EU experience in the context of business collaboration with industry associations;
- improving institutional support as a part of achieving compliance with EU standards on sanitary, phytosanitary and environmental requirements;
- facilitating of solving the problems of the geographical indications with the active involvement of the EU experience and resources;
- direction of the Agreement for Reform in Ukraine.

For Ukraine, the opening of the European market in the context of the Association Agreement with the EU is certainly important and necessary for its further integration into the global economy. Crucial for Ukraine is not only increased access to European markets, but also the exploitation of signing the Agreement opportunity for reforming and improving the competitiveness of the national economy that will ensure the growth of export of Ukrainian high-tech products, and thus creating conditions for increasing employee salaries based on improved performance labor and thus growth in consumer demand in the domestic market. Particularly important in this process is to ensure the inclusion of certain activities in the process chains of industrial production of the EU, many of which are actively implement the new industrial strategy (Heyets et al., 2014, p. 102).

Regarding to the domestic business, the DCFTA will allow Ukrainian companies to participate in EU public procurement. Admittedly, the list of industries today, where representatives of Ukraine will be able to open a business in the EU is quite limited – postal and courier, financial and telecommunication services. Bringing the national legislation into line with the EU opens our business access to European markets. On the other side, as a result of the approximation of the laws of EU investors in these sectors have the same legal right to work in Ukraine, as in the EU.

The important task for Ukrainian exporters to the Community will be given to the application of rules of origin of the European Union that will provide bilateral cumulation of origin between Ukraine and the EU. Nowadays Ukraine benefits from unilateral trade concessions from the EU in the form of GSP. Abolition import duties applies to 94,7% of total manufactured goods and 83,4% of agricul-

tural goods and food products imported from the EU from our country. The preferences will be valid until January 1, 2016 (Creation of free trade zone between Ukraine and the EU). However, steel, textiles and clothing, fertilizers are in understated rates. When the DCFTA will come into effect completely, preferences lose strength, and tariffs will be eliminated.

For all the provisions of the Association Agreement were acted and all the commitments were made, in the text the multilevel system coordination of efforts is underlined, the Summit, the Council of Association, Committee Association, Parliamentary Committee Association and Civil Society Platform, which will consist of members of the European Economic and Social Committee and representatives of civil society in Ukraine.

Implementation of the Agreement on the successful cooperation of the Government of Ukraine, the Supreme Rada and business can provide the following prospects for our country (see table 4).

Table 4

**Prospects for Ukraine related to the Association Agreement with the EU\***

№	Prospects	Arguments
1.	Better access to big market.	The EU is the largest single market in the world, consisting of 28 countries and covers the population, which is 11 times higher than the population of Ukraine. It is over 500 million consumers, whose average income is 39 thousand dollars USA.
2.	Lower import duties for Ukrainian goods.	One of the main consequences for companies FTA+ will cancel import duties for 97% of all goods exported from Ukraine to the EU. Only 3% of exports of certain agricultural products import duties will not be completely canceled.
3.	Access to public procurements in the EU countries.	Legislation and procedures in public procurement will allow Ukrainian companies to participate on equal terms with European enterprises in the work conducted by state order, services and in conducting tenders at EU level. The volume of the market is almost 2,5 trillion dollars USA.
4.	Lower prices and higher living standards.	Ukraine will reduce tariff rates on imports from the EU. Manufacturers in Ukraine will have access to a wide range of cheaper industrial products, components and equipment. The standard of living in a few years will grow by 12%.

№	Prospects	Arguments
5.	Better access to the markets of third countries.	Better access to the markets of third countries will be provided by harmonizing technical regulations and standards in accordance with EU requirements, which also involve the prospect of recognition of the Ukrainian goods to the markets of the USA, Japan, Canada and Korea.
6.	Reform foundation.	Bringing Ukrainian legislation in many areas of commercial activity with EU requirements will set timetable improve the domestic investment climate and the transition to a more transparent business rules that would have made domestic economic environment more attractive for foreign and domestic investors.
7.	Ukraine will maintain the independence, sovereignty, identity.	The development of closer relationships with other countries and multinational alliances is the sovereign decision of Ukraine and its people. Implementation of common rules and standards for Ukraine will not mean loss of independence, sovereignty, their customs and individuality.
8.	European integration will positively affect the economy of Ukraine.	The Association Agreement provides an opportunity to benefit from practical assistance to the EU and its experience of reforms that have helped many countries to modernize, to provide higher standards of living for its citizens and to reach the highest technological level of development.

\*Prepared by the author based on (The principles of the Association Agreement between Ukraine and the EU on free trade zone).

Ukraine inspires confidence in the European choice of development and future prospects of the fact that, thanks to the growing power of the EU, already in the first third of the XXI century, the formation of the global market with three major continental markets – European, North American and Asia-Pacific will complete. Thus, we can argue about the decisive influence of the EU to build a new world economic order.

**Conclusions.** Successful implementation of the Association Agreement and its implementation will mean the parties correspondence to the criteria of EU membership, which is the goal of Ukraine. Through FTA + with the EU Ukrainian producer is able to find a niche on the European market and domestic consumers – access to high quality European products at affordable prices. FTA + with a focus on regulatory cooperation – is the institutionalization of contractors conver-

gence of international trade, represented by the creation of appropriate structures of authority and a clear pattern of interaction will contribute modification of competitive relations in the plane of the Ukraine – EU will be supranational institutional support DCFTA. It is clear by the fact that the process of adaptation to the conditions of the state and DCFTA will be difficult, but the prospect of improving the investment attractiveness – a unique platform for developing mutually beneficial relations between the parties, as well as growing confidence to Ukraine from developed countries.

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