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Ukraine and the European Union: Selected trade issues

After its enlargement in May 2004, the EU became the largest trade partner of Ukraine. Trade with the EU-25 is estimated to account for 30% of the merchandise exports and 32% of imports in 2004. Ukraine primarily exports ferrous metal products, fuels, and some machinery to the EU. In return, its major imports are machinery, equipment, and chemical industry products. Today the EU is a prime provider of investment goods for Ukraine.

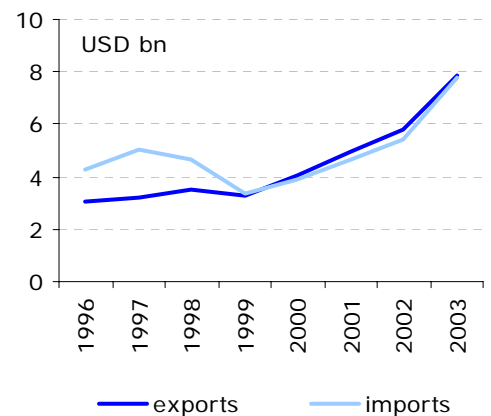
However, despite the large volumes, Ukraine's trade relations with the EU are complicated by a number of trade restrictions. Regarding tariffs, Ukraine and the EU granted each other Most Favoured Nation status (MFN), which, however, implies the highest possible tariff rates for the EU. In addition, Ukraine is a beneficiary of the EU's Generalized System of Preferences (GSP). However, the scheme for Ukraine excludes iron and steel, fertilizers, fishery products, and grains, seeds, fruits and plants, i.e. some of Ukraine's most important export products. Moreover, the GSP provides rather small tariff reductions for sensitive goods, including most agricultural and food products, textiles, and some chemicals and non-ferrous metals. The Partnership and Cooperation Agreement between Ukraine and the EU doesn't give any additional trade preferences to Ukraine, whereas most other EU trade partners enjoy far more favourable trade regimes, including free trade or association agreements, thus having additional tariff preferences, which Ukraine doesn't possess. Before starting negotiations on a free trade agreement with the EU, Ukraine has first to become a member of the WTO.

In addition to tariff barriers, Ukraine and the EU are involved in trade disputes. As of the end of 2003, Ukraine was subject to 8 definitive anti-dumping duties, directed towards chemical products and ferrous metal products, in particular tubes and pipes. An additional problem related to anti-dumping measures against Ukraine is the country's non-market-economy status, which deprives Ukrainian enterprises of an effective defence of their rights in EU-initiated investigations (though in 2000 EU allowed a "market economy enterprise" status for firms that can substantiate that they operate under market economy conditions). It is presumed that in a non-market-economy prices are distorted and thus cannot be used to investigate violations of market competition. As a result, investigators use third-country prices as indicative, limiting the enterprises' defence possibilities, and resulting in higher anti-dumping duties than otherwise would be.

According to EU legislation, the criteria that allow a country to obtain market-economy status include the degree of government influence, the absence of state-induced distortions in the operations of enterprises, the existence and enforcement of transparent and non-discriminatory company legislation, a coherent, effective and transparent set of other laws, and the existence of a genuine financial sector. Ukraine has applied for market-economy status several years ago, but has not obtained it so far. The major concerns of the EU are state intervention in the price formation mechanisms and inappropriate bankruptcy rules. However, it is expected that the election of Viktor Yushchenko to the presidency, will bring about policy changes that will allow the EU to grant market-economy status to Ukraine. This status is likely to be granted conditionally, i.e. prior to actual changes, allowing the EU to send a positive signal to Ukraine, while at the same time giving the new government time to resolve the EU's outstanding concerns.

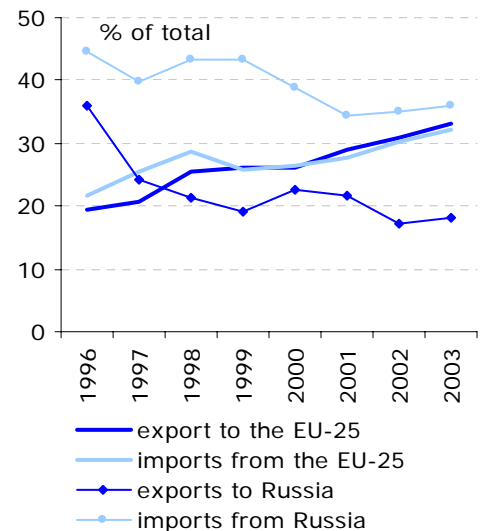
Improving Ukraine-EU relations, which inevitably affect trade, were reflected in the European Parliament's January resolution calling for Ukraine to be given "a clear European perspective, possibly leading to EU membership". Although the European Commission is much more cautious, it also promised to intensify relations with Ukraine, including trade.

Merchandise Trade with the EU-25



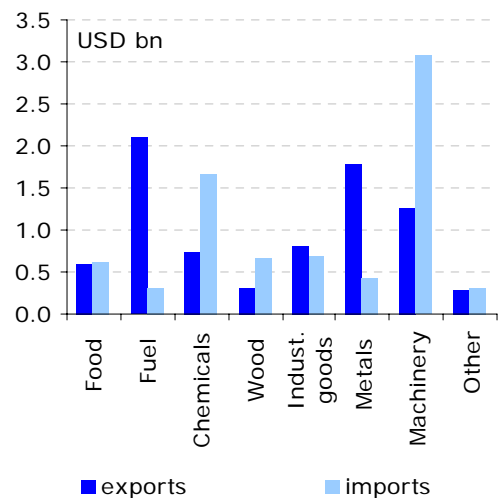
Source: NBU

Trade with the EU-25 vs. Russia



Source: NBU

Structure of Trade with the EU-25



Source: NBU

Author:
Veronika Movchan
Institute for Economic Research and
Policy Consulting


Quarterly Trends

National accounts **		Q2 02	Q3 02	Q4 02	Q1 03	Q2 03	Q3 03	Q4 03	Q1 04	Q2 04	Q3 04
GDP	UAH bn	49.9	64.1	63.3	51.5	60.0	75.6	77.1	64.1	78.6	101.0
GDP (real)	% yoy	4.7	4.3	6.1	8.4	10.0	6.8	12.1	12.3	13.2	14.2
Households consumption (real)	% yoy	2.0	8.9	11.2	10.2	14.4	11.2	13.6	15.5	16.0	15.6
State consumption (real)	% yoy	5.4	-18.8	2.9	15.0	17.8	19.2	9.0	-3.6	-2.0	-3.0
Gross fixed capital formation (real)	% yoy	7.8	3.8	5.7	9.0	20.4	24.3	9.0	23.3	4.3	6.1
Exports of goods and services (real)	% yoy	2.5	15.3	17.0	9.9	9.8	9.8	11.6	16.5	15.2	6.2
Imports of goods and services (real)	% yoy	1.4	10.4	6.7	13.8	16.2	17.4	17.7	14.5	7.0	4.3
Agriculture, hunting, forestry (real)*	% yoy	12.1	2.1	1.3	4.0	-13.7	-22.5	6.7	-4.2	1.2	36.2
Manufacturing industry (real)*	% yoy	10.6	8.0	11.5	12.0	15.4	23.0	20.1	22.7	15.5	13.8
Construction (real)*	% yoy	-7.9	-1.2	2.7	18.2	24.8	30.9	16.9	29.8	30.6	17.2
Trade, repair services (real)*	% yoy	5.3	8.8	3.5	7.2	15.1	22.6	29.6	23.5	35.1	3.0
Transport (real)*	% yoy	0.5	7.9	11.0	10.0	11.5	15.9	11.7	11.0	8.9	11.1
Balance of payments											
Current account balance	USD bn	0.6	0.8	1.0	1.1	0.7	0.7	0.4	1.7	2.3	1.7
Current account balance	% of GDP	6.7	6.4	7.9	11.2	7.0	5.0	3.0	14.3	16.5	9.7
Trade balance in goods	USD m	87	155	225	309	-42	-155	-381	767	1460	683
Trade balance in services	USD m	244	247	382	387	399	362	409	542	307	549
Current transfers	USD m	441	517	520	500	526	574	584	465	746	703
Direct investment (FDI)	USD m	119	156	300	238	454	390	329	310	574	388
Portfolio investments	USD m	-311	-592	-520	-825	640	-444	-293	60	-409	779
Gross international reserves	USD bn	3.4	4.1	4.4	4.6	6.2	6.7	6.9	7.9	9.6	12.1
Fiscal indicators											
Consolidated fiscal revenues	% of GDP	29.9	28.2	28.1	31.6	31.7	30.1	28.6	27.2	26.9	26.3
Personal income tax	% of GDP	5.2	4.9	4.9	5.7	5.7	5.3	5.1	4.4	4.1	3.8
Enterprise profits tax	% of GDP	4.3	4.1	4.3	5.7	5.1	4.8	5.0	3.9	4.0	4.1
Value-added tax	% of GDP	6.6	6.4	6.1	6.2	6.3	5.8	4.8	6.2	5.7	5.1
Excise tax	% of GDP	1.9	1.9	1.9	2.1	2.2	2.1	2.0	2.1	2.1	2.0
Consolidated fiscal expenditures	% of GDP	28.4	26.4	27.3	27.7	29.2	27.9	28.8	25.3	26.5	26.8
Current expenditures	% of GDP	na	na	na	na	26.3	24.2	24.3	22.4	22.7	21.7
Capital expenditures	% of GDP	na	na	na	na	3.0	3.7	4.4	2.9	3.8	5.1
Consolidated fiscal balance	% of GDP	1.5	1.7	0.7	3.8	2.5	2.2	-0.2	1.9	0.4	-0.5
Privatisation receipts	% of GDP	0.4	0.3	0.3	0.6	1.0	1.0	0.8	1.5	3.7	3.5
Labour market											
Average wage (real)	% yoy	20.0	21.2	17.7	12.3	19.1	19.9	14.9	23.0	17.8	13.2
Household income (real)	% yoy	61.3	100.8	65.6	-1.2	8.6	10.0	8.7	15.7	13.0	9.9
Unemployment rate (ILO methodology)	%	9.7	9.2	11.1	9.4	8.8	9.2	9.0	9.7	7.9	6.1
Banking system											
Monetary aggregate M0	% yoy	48.0	46.0	35.8	32.4	37.0	30.5	25.3	29.1	25.6	37.1
Monetary aggregate M2	% yoy	39.5	46.5	42.2	47.8	54.6	49.9	47.6	45.4	44.8	51.5
Household deposits in national currency	% yoy	90.1	103.6	72.5	73.4	74.7	65.0	66.1	69.4	67.3	67.9
Household deposits in foreign currency	% yoy	47.4	55.1	59.3	71.2	70.2	70.4	77.5	67.0	61.7	55.2
Com. bank credits in national currency	% yoy	34.5	42.3	54.4	63.7	71.2	73.0	61.7	56.8	52.1	44.3
Com. bank credits in foreign currency	% yoy	32.1	37.3	40.3	44.1	48.4	57.7	60.9	63.6	56.2	43.5
Long-term com. bank credits	% yoy	70.6	85.8	92.5	110.6	156.4	164.0	157.9	141.7	102.7	82.7
Long-term com. bank credits	% of total	23.5	25.3	28.2	31.3	37.4	40.1	45.0	47.4	49.3	50.9
Average lending rate on national cur. credits	% p.a.	25.0	23.5	21.8	18.0	17.2	17.2	17.7	17.2	16.6	17.0
Average lending rate on foreign cur. credits	% p.a.	12.9	11.9	11.3	12.5	12.6	11.7	10.9	12.2	12.1	12.6

SOURCES: National Bank of Ukraine, State Committee of Statistics, State Treasury, Ministry of Finance, IER estimates

* change in value added

** preliminary

Notes:
yoy year on year change

p.a. per annum