Assessment of the impact of
the Association Agreement / DCFTA
between Ukraine and the EU
on Ukraine's economy

Scientific report

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SUMMARY

For Ukraine, opening of the European market and the signing of the Association Agreement with the EU is definitely important and vital to ensure its further integration into the global economic space. The preconditions for the successful integration of the Ukrainian economy into the world community are the solution of a number of problems. The key to this is to ensure that there are positive changes in the structure of the national economy, and related structural reforms. To date, the economic integration of Ukraine is characterized by the absence of broad industrial and technological relations with the EU. As a result Ukraine's exports are represented mainly by products with low processing degree. At the same time finished products are imported to Ukraine from the EU, including investment purpose products with higher added value. Therefore, it is crucial for Ukraine not only to improve the access to European markets, but also to use the opportunities for reforming and improving the competitiveness of the national economy derived from signing the Agreement. This should ensure the growth of Ukrainian exports of high-tech products, thus creating the conditions for the growth of workers' wages through improved labor productivity and, hence, growth in consumer demand in the domestic market. It is particularly important in this process to ensure the inclusion of certain activities into manufacturing chains of industrial production of the EU countries, many of which rapidly implement new industrial strategies.

Changes in the trade regime as a result of Ukraine signing the Agreement will act in the short term. They will be expressed primarily in changes of the existing trade regime by abolishing the EU import duties for Ukrainian goods, and the gradual reduction of Ukraine's import duties on goods from the EU over the next five years (Appendix A, B to the Agreement).

The Agreement also provides for the deepening of cooperation by involving Ukrainian business entities into general research, communication and information projects (which falls under Sections IV "Trade and Trade-related Issues", and V "Economic and industrial cooperation" of the draft Agreement). Given the relatively high scientific and technological potential of Ukraine's economy, the growth of Ukrainian exports of certain types of high-tech products and services can be expected.

Implementation of the Agreement from January 1, 2014 could have laid the ground for the following macroeconomic effects in annual terms: output growth by 20.6 billion UAH; GDP - by 11.1 billion UAH in constant prices in 2010 (1.0%); exports - by 11.9 billion UAH (2.4%); imports - by 8.2 billion UAH (1.2%); so that private consumption could grow by an additional 3.7 billion UAH (0.7%); and investments - by 0.8 billion UAH (0.5%).

For individual sectors of the economy of Ukraine, the signing of the Agreement in 2013 could have resulted in the following changes in output volume:

- In the real sector: *an increase in output* *in agriculture* (3.1 billion UAH); *food industry* (3 billion UAH); *light industry* (1.2 billion UAH); *mining* (1.1 billion UAH); *wood working* (0.7 billion UAH); *metallurgy* (2.2 billion UAH); *mechanical engineering* (1.0 billion UAH); ***a decrease in output*** *in chemical industry* (by 0.9 billion UAH already in 2014 and up to 4.0 billion UAH in 2018) due to higher share of imports from the EU, compared with exports to the EU, import volumes will grow faster;

- In the service sector: *the highest growth of volumes* *in hotel and restaurant business* (1.5 billion UAH); *informatization* (1.9 billion UAH); *financial activities* (0.9 billion UAH); *and activities in the fields of law, accounting, engineering, services for businessmen* (0.8 billion UAH).

Failure to sign the Agreement on November 28, 2013 has delayed liberalization of trade regimes for Ukrainian exporters. This has made it impossible for cost savings through the abolition of import duties. Today we can talk about the loss of potential opportunities for Ukrainian producers in the EU markets by the end of 2014.

The lost economic opportunities from January to April 2014 are macroeconomic in nature. They cannot be considered only as export losses, as they are expressed in the decrease in the expected growth of: output by 7.0 billion UAH (0.33%); GDP - by 3.7 billion UAH (0.36%); private consumption - 1.2 billion UAH (0.23%); GFCF - by 0.3 billion UAH (0.16%); exports of goods and services - by 4.0 billion UAH (0.8%); imports - by 2.7 billion UAH (0.4%); including *in agriculture* - by 1.0 billion UAH; *food industry* - by 1.0 billion UAH; *light industry* - by 0.4 billion UAH; *mining industry* - by 0.3 billion UAH; *wood working industry* - by 0.3 billion UAH; *metallurgy* - by 0.7 billion UAH; *mechanical engineering* - by 0.3 billion UAH; *hotel and restaurant business* - by 0.5 billion UAH; *informatization* - by 0.6 billion UAH; *financial activities* - by 0.3 billion UAH; activities in the field of law, accounting, engineering, services for businessmen - by 0.3 billion UAH.

ASSESSMENT OF THE IMPACT ON CERTAIN ECONOMIC SECTORS AND COMMODITY MARKETS

Agriculture

Benefits

The main positive point of the free trade area (FTA) with the EU in terms of trade in agricultural products is the partial removal of asymmetry in terms of trade between the EU and Ukraine, which strengthened after Ukraine's accession to WTO. The asymmetry is reduced by: duty-free access for Ukrainian agricultural products within the framework of tariff quotas; EU's refusal to use export subsidies on agricultural products for export to Ukraine; and establishing the right of Ukraine to the use of protective measures and additional trade terms.

In the crops market, the unambiguous positive for export expansion is the introduction of quotas on grain exports to the EU at a zero import duty rate. As a result of the creation of the deep and comprehensive FTA in accordance with the Association Agreement between Ukraine and the EU, Ukraine will be able to supply duty-free to the EU 1.6 million tons of cereals. At the same time a gradual increase in quotas up to 2 million tons over five-year period is provided. The quota for import of wheat into the EU will be set at 950 thousand tons, after which it will be increased to 1 million tons, barley - 250 thousand tons increasing to 350 thousand tons, and corn - 400 thousand tons and 650 thousand tons in five years. Currently, Ukraine exports cereals to the EU on general terms; therefore, allocation of the personal quota for Ukraine can be considered a positive fact.

Challenges

Growth of exports of domestic agricultural products to the EU market will be constrained due to: the small volume of EU import tariff quotas for duty-free import of products from Ukraine; and the current inability of the majority of domestic manufacturers to meet the technical, sanitary and phytosanitary conditions for exporting their products to the EU markets.

There is a danger of weakening the competitive position of domestic producers of meat and meat products, dairy products, fruits and vegetables as a result of the growth of imports from the EU. According to our calculations, annual imports of pork and poultry meat from the EU to Ukraine after the establishment of the FTA with the EU will increase by 22.4% and 6.1% respectively. Therefore, the annual sales volume of domestic producers in the domestic pork market will shrink by 4.89 thousand tons. The share of EU imports of pork into Ukraine will increase from 35% to 39%. Poultry producers will need to further increase their exports by 1.8% in order to compensate for the decrease in sales volume in the domestic market as a result of abolition of trade restrictions.

The total costs of the modernization of livestock production and vegetable production facilities up to EU standards is estimated at about 900 million Euros over the 10 years of the implementation of the Association Agreement.

As a result of the FTA with the EU, the CU/SES countries may resort to trade restricting measures, in particular with respect to agricultural and food products. They might introduce:

- non-tariff restrictions on imports of goods from Ukraine, which represent the largest share of Ukrainian agricultural exports (cheese, sunflower oil, chicken, pork, beef, alcoholic and soft drinks and confectionery);
- protective measures in the form of additional duties on Ukrainian export goods, or change of the customs regime in the event of forced exit of Ukraine from the CIS free trade area.

Total losses of exporters from the introduction of restrictions on trade in agricultural products by the CU/SES states through signing the Association Agreement between the EU and Ukraine could exceed 440 million US dollars.

Industry

Ferrous industry

Benefits

The signing of the Association Agreement with the EU provides for the abolition of duties on the products of domestic steel producers. In the short term this will cause a slight (0.4%) increase in metallurgical production output and production of finished metal. As a result of the abolition of duties on certain commodity groups of ferrous metals a slight increase in export revenues of domestic steel producers is expected within the range of about 25-30 million Euros. There is a possibility of avoiding trade restrictions (antidumping duties), and there might be a slight increase in export revenue for domestic pipe producers in the range of 30 million Euros.

Challenges

Despite certain advantages, the Association Agreement with the EU includes certain risks, associated primarily with the need to increase the cost of reducing the harmful impact of steel production on the environment. Another threat to domestic steel producers (under the worst case scenario) is the full closure of the metallurgical market with the CU/SES. This will lead to overproduction of domestic steel products within the range of 3.6 million tons, which are currently exported to CU/SES countries. Also, according to our calculations, in the medium term we expect a slight (0.2%) reduction in steel production.

Mechanical engineering industry

Benefits

The opportunity arises to accelerate modernization of the domestic mechanical engineering industry through the use of scientific and technological achievements of European countries. Currently, almost 30% of new technologies and equipment that are used in the modernization of Ukrainian industry are purchased outside Ukraine. Also, domestic production can be adapted to technological, health and environmental standards of European countries; zero import duty rates can be established on investment types of engineering products.

On average, the rate of import duty on vehicles that come from Ukraine is reduced by 30%. This will improve the competitiveness of the domestic products.

Challenges

The likelihood is growing of an increase of competing imports in the Ukrainian domestic market, in particular with regard to cars, tractors, and combine harvesters.

The barriers for domestic producers to enter the European market remain relatively high, as Ukraine is at the lower level of technological development than EU countries. This is confirmed by the share of exports of high-tech products (as a percentage of total exports of industrial products) by Ukraine and individual EU countries: Ukraine - 5%, Hungary - 29%, Finland - 21%, Sweden - 17%, France - 19%[1].

The dependence of domestic mechanical engineering industry on imports of high-tech products is growing, both in terms of end products and components used for the assembly of cars of famous foreign brands. The evidence of this is the growing demand for innovative high-technology engineering products. In 2013, the volume of imports of mechanical engineering products was 1.4 times higher than domestic production volume.

Woodworking industry

Benefits

Ukraine has great potential as an exporter of wood products, and the EU is the largest foreign market for products of this industry. According to forecasts of the UN European Economic Commission, in 2015 the deficit of round wood in the European Union countries will amount to 77 million cubic meters, lumber - 8.1 million cubic meters, and wood fiber semis - 7.7 million

[1] *Source: calculated on the basis of WordDevelopmentIndicators: [electronic resource]. — Access mode: <http://data.worldbank.org/indicator/TX.VAL.TECH.CD>.*

tons. This indicates that there are prospects for economic cooperation between Ukraine and the EU in expanding the foreign wood products market.

Challenges

There is a possibility of increased imports of products with high added value (board products, joiner and carpenter products, structural components). Their share in the import of wood products was more than 75% in 2013.

On the other hand, the trend of increase of commodity exports will improve. The share of raw timber and lumber in the structure of exports to the EU during 2008-2013 was fluctuating around 50%.

Food industry

Benefits

After implementation of the FTA with the EU, a significant reduction or gradual elimination of tariffs on industrial food products (about 85% of tariff lines) not covered by tariff quotas will take place. Ukraine has the opportunity to reduce its import duties over a period of up to 10 years depending on the type of food products.

Ukraine will be entitled to duty-free access within the framework of allocated tariff quotas to European markets of milk, dried and condensed milk, cream, yogurts, butter and milk paste, sugar, syrups, juices, starch, flour, and some other kinds of foods, as well as cigarettes and cigars.

After creating the FTA with the EU, subject to an appropriate investment climate, an increase of investment in the domestic food industry from the EU countries can be expected.

The domestic confectionery industry has great potential to increase export sales after the creation of the FTA. Following the liberalization of foreign trade and WTO accession by Ukraine, the increase of exports of sweet biscuits and waffles, chocolate and sugar confectioneries to the EU, and the minimal amount of expansion of imports in the domestic market were recorded. This evidences the high competitiveness of the domestic confectionery industry; and its potential with the FTA to increase exports to the European market, and to withstand the competitive pressure from imports in the domestic market.

Among soft drinks producers, the opportunities to increase exports to the EU after the creation of the FTA are open for fruit and vegetable juice producers. Mineral water and other soft drinks producers have little export potential in the EU, as after Ukraine’s accession to the WTO they failed to increase exports. However, it is unlikely that the expansion of imports from the EU after the establishment of the FTA will reduce their share of the domestic market.

Challenges

There is a danger of weakening of the competitive position of domestic food and processing industry enterprises, especially small and medium-sized, in view of the increasing competition in the domestic market.

Against the background of EU high non-tariff barriers for the domestic food industry, the special risks for the industry are posed by the likely loss of the CU/SES markets, in particular Russia. The minimum loss of export earnings in the food industry could reach 147 million US dollars per year.

Manufacture of textiles and clothing

Benefits

After signing the Agreement, the EU is going to set to zero the import duties on textiles and clothing. Ukraine will have a transitional period to change the rates for EU goods - gradually reducing the import duty in textile production to 0.1%, and in clothing manufacture to 0.2% of the customs value. There will be an adaptation period for Ukrainian producers. At the same time, imported Polish clothing for consumers will be cheaper, equaling the prices of Turkish products.

Challenges

The risk of increased imports of second-hand clothing as a result of reduction of import duty over the five year period is to be neutralized by special input prices in Euros per net weight kilogram. Even today, with Ukraine’s base rate of 5.3% there is a sharp increase of second-hand imports from other countries, the share of EU imports remains high (84.8%). Establishment of a single customs checkpoint for second-hand clothing and introduction of quotas for a single recipient can also occur.

Footwear industry

Benefits

After signing the Agreement, shoes from the EU will be imported to Ukraine without 10% import duty, which is currently applicable. Abolition of the duty will not have a material adverse effect on the operation of domestic enterprises. This is because in recent years up to 90% of footwear from the EU and other regions is imported into Ukraine through shadow schemes. The gradual elimination of import duties in the EU (currently 8% to 17%), and other trade barriers will increase the supply of Ukrainian shoes in the European Union.

Footwear safety (except special shoes and protective shoes with specific functions) in the EU is ensured through monitoring of safety of materials used for its manufacture. The requirements for materials set by the EU are similar to those in Ukraine. In the field of footwear production there are no mandatory EU standards and special EU regulations.

It is positive that after signing the Agreement, apart from increasing the volume of footwear exports to the EU market, Ukraine will obtain access to the highest European technology (high-tech equipment, modern materials and raw products, chemicals for leather and footwear production), currently lacking in the domestic footwear industry.

Challenges

When creating the FTA between Ukraine and the EU, there is the risk of politically motivated sanctions against Ukrainian shoes from certain CIS countries.

Power industry

Benefits

The Association Agreement between Ukraine and the EU consolidates commitments that have been made earlier under the European Energy Community. It sets a clear schedule for their implementation from the effective date of the Agreement. These commitments provide for implementation of a number of European directives aimed at transforming: the institutional environment in electricity and natural gas markets (directives of the Second and the Third Energy Package); the technical and technological structure of production capacities and energy balance as a whole (Energy Efficiency Directives, promotion of renewable energy sources (RES); and the limitation of emissions of harmful substances. The objectivity of the motivational factors of the reforms stipulated by international obligations must be recognised, as well as the non-discriminatory nature of these agreements. The progress in stabilizing the energy supply of the economy, and integration of the energy sector of Ukraine with continental energy markets, will depend solely on the effectiveness of implementation of internal reforms and adequate financial support.

Challenges

The most financially significant block of commitments is the implementation of energy efficiency projects. The total cost (including non-consumption expenditures of the population) in order to achieve energy efficiency targets up to 2020 could reach 86.0 billion Euros. The general cost of infrastructural commitments up to 2020 could reach 100.7 billion Euros (in addition to the investments provided for by the Energy Strategy of Ukraine up to 2030).

More than half the cost of the energy efficiency policy should fall on the household sector, where the potential for energy savings is the most economically justified. The ability to achieve targets to reduce final energy consumption will therefore depend on the effectiveness of implementation of interconnected systems of clear price signals, and compensation arrangements established with participation of the State.

In the industrial sector, implementation of energy efficiency projects will increase the capital intensity of production by an average of 30%. The average cost of electricity will increase as a result of the obligation to comply with environmental standards, and also the increased share of renewable energy generation. In the short term this will put additional pressure on industrial producers' output. The intermediate consumption of which, to a significant extent, consists of products of industries which are recipients of investment resources. At the same time it is obvious that intensification of the investment process up to 2020 will help to maintain the competitive advantages of Ukrainian goods in the long term. This is because it would reduce the investment needs of the industry during 2021-2030 by 10.2% and energy intensity of industrial production by 19.5%.

There are additional obligations that are not currently established in the Association Agreement, but are expected in the format of the Energy Community (the Third Energy Package, the new Energy Efficiency Directive). They can radically enhance the economic effects, so their adoption should be preceded by thorough scientific expertise and professional development of Ukraine's position.

Transport infrastructure

Railway transport

Benefits

The ability to import the new technologies and technical solutions for modernization and re-equipment of rolling stock and railway transport facilities will grow. This is subject to scientific and technical cooperation with the EU countries having experience in the development of speed and high-speed transport.

The competitiveness of domestic railway transport will improve due to implementation of EU legislation in the field of technical regulation.

The introduction of two EU regulations on passenger transport will stipulate raising of railway passenger safety standards and lead to observance of the European principles and rules of refunds in case of passengers death or injury.

Challenges

One of the first Directives on railway transport to be introduced in Ukraine was adopted by the EU in 1991. The total period of implementation of these directives in the EU countries has been 21 years. Ukraine, unlike the EU member states, has to implement these directives not step-by-step, but simultaneously. In accordance with the Association Agreement, Ukraine has only eight years to implement all the above EU Directives into the national law. This is unacceptable in the current context of Ukraine railway transport reforms.

Uncertainty with the status and organizational structure of Ukrzaliznitsi is due to the fact that the process of reforming the railway transport of Ukraine from 2012 only began with the adoption of the Ukraine Law No. 4442-VI "On the specifics of creating of the public joint stock company of railway transport of public use" dated February 23, 2012. Pursuant to this, the Cabinet of Ministers of Ukraine had to decide on the formation of a public joint stock company of public railway transport within three months, which is by June 2012. Presently, in the middle of 2014 this legal act has not yet been adopted.

The EU directives make demands to limit the management model of railway transport in the countries that have implemented them. In addition, the fourth EU railway package aimed to prohibit, in 2012, the holding model of railway transport management in the EU countries in general, and to begin a large-scale privatization of the railway network.

Labor market

Benefits

The consequence of trade liberalization is the creation of a more favorable business environment and investment climate, and the liberalization of the conditions for setting up a business. There is the prospect of intensification of entrepreneurship and the creation of new jobs in agriculture, chemical, food, light industry.

The mode of far-reaching liberalization of trade in services offers the prospect of increased employment in the service sector, particularly in trade, tourism, communications, IT-sector, engineering, media, market research, and employment activity.

New jobs in the power industry, transportation, construction, and municipal services are expected as a result of the implementation of projects of modernization of the energy, transport and municipal infrastructure. This will occur in the framework of cooperation between Ukraine and the European Investment Bank, and the European Bank for Reconstruction and Development.

Challenges

At the same time there is a threat of increased unemployment as a result of the closure of uncompetitive and unviable industries. Initially, the workforce may be reduced in mechanical engineering (automotive, shipbuilding, machinery and equipment).

As Ukraine is lagging in terms of wages, one of the major risks is the possible movement into other countries of skilled workers, entrepreneurs, as well as young people studying abroad. This can happen if it is provided by sectoral agreements and by the expansion of access of Ukrainian citizens to the new flexible EU immigration schemes, which are available to third country citizens and their family members.

The terms of the Agreement do not provide for freedom of labor movement, and the creation of a common labor market between the EU and Ukraine. The risk of an increased flow of illegal migration of Ukrainians to the EU is therefore growing. Also the risk is growing of increased input flows of migrants and refugees from third countries in transit to the EU.

Financial sector

Benefits

Assessing the prospects of enhancing the integration process of Ukraine with the EU for Ukraine's financial sector, it should be noted that the national financial sector needs qualitative transformations. This need is objective. At the signing of the Agreement there is an opportunity to provide more intensive and better convergence with the European policy of development and regulation of financial markets. On the other hand, in order to ensure the real quality of such large-scale transformations, the main task of public policy is the prevention of the risk of further consolidation of the adverse profile of national financial intermediation as a mechanism for servicing foreign capital inflows and restriction of sovereignty in monetary policy matters.

The advantages of Ukraine's currency integration with the EU countries will include: reducing the dependence of cash turnover on the US dollar; improvement of the currency structure of the international reserves of the NBU and external debts; development of credit cooperation with the EU; increase of the market of liquidity of the European currency in Ukraine; entering direct quotations of Euro against the hryvnia.

Challenges

The poor integration of the domestic financial market with the international one, and underdeveloped financial infrastructure in case of increased openness, make the financial market vulnerable on many fronts, including: on the inflow of speculative foreign capital, import of crises, and greater dependence on international financial institutions.

One of the problems of convergence with the EU also lies in different macroeconomic conditions of Ukraine and most EU member states. On the one hand, low macroeconomic indicators in Ukraine (GDP per capita, level of wages), on the other hand the underdevelopment of financial markets (capitalization of banks, terms of provision of financial services, financial markets liquidity, volume of financial services provided, and availability of funding) put domestic financial companies at a disadvantage compared to the European ones entering the Ukrainian financial market.

The opening of the financial market of Ukraine brings certain risks associated with the possible influx of foreign capital in the form of both direct and portfolio investments. Primarily the foreign exchange market of Ukraine may be within the risk zone. In the face of a possible influx of large amounts of investment, the hryvnia exchange rate will be under pressure of revaluation processes. Ukraine already had such an experience in 2007, when the influx of foreign capital grew by almost 3.5 times as compared to 2006. The conversion of foreign currency in the domestic foreign exchange market contributed to revaluation of the hryvnia by almost 8%. With regard to portfolio inflows, they are unlikely to come in large volume after the signing of the Agreement.

Taking into account the content of the revision of the economic part of the Association Agreement between Ukraine and the EU, the absolute introduction of the provisions of numerous euro directives in the field of securities is stipulated within four years after the Agreement enters into force. For a long time the compliance with euro directives in regulatory policy was mostly declarative and selective rather than systematic and consistent. Therefore the implementation of European regulations, in particular in the stock market, will be associated with numerous difficulties both for market entities and for the regulator.

Institutional environment

Technical regulation

Benefits

The introduction of technical regulations in Ukraine according to EU requirements will ensure the compliance of domestic policies and procedures with European regulations and procedures. The certified products will be treated as compliant with EU requirements, and will not require additional checks. Ukraine has commitments on technical regulation of industrial products according to international standards and legislative implementation. As a result, technical regulations and standards in various industries will be an important signal for strategic foreign investors for the organization of new production facilities and new jobs in Ukraine.

Challenges

The introduction of the EU technical regulations may create some technical barriers for goods from Ukraine to the EU market. The EU technical regulations cover the goods from such UKTVED industrial groups as: 04, 09, 11, 15-24, 50-63, 84-85, 87, 90.The total value of exports of these groups is 3.9 billion US dollars.

The transition to EU technical regulations will also require significant financial commitments from industrial plants for the modernization and re-equipment of production, and development of new technologies. In addition, the harmonization and adaptation of national legislation to European standards regarding technical regulation requires the state to develop an effective control system. It must be built on international and European experience, which has to shield the domestic market from low-quality and counterfeit products, including foreign ones.

Government aid

Benefits

The introduction of state aid control in accordance with the Association Agreement between Ukraine and the EU will enhance the transparency of decision-making on granting of state aid. This includes through the procedure of the control of legality of its provision, which stipulates that when unlawful aid is revealed, the company is obliged to return the provided funds to the state, as well as compensate for other losses in the form of penalties and interest.

The regulation of state aid, according to the Agreement, will contribute towards reduction of the amount of government aid. There will be a corresponding reduction of budget expenditures as a result of abolition of those aid forms that are the most adverse for the competition.

Challenges

The potential danger is the narrowing of space for the application of measures of state aid to enterprises. Government support for the coal industry, construction, and shipbuilding may be subject to abolition or restriction. Abolition of certain state aid measures for enterprises that previously enjoyed them may possibly affect adversely economic development. In addition, the tools for support of domestic producers that compete with higher-quality goods from the EU will be lost.

Due to the need for creation of a new supervisory element, the bureaucratic procedures in the approval of new state aid measures will become more complicated. Budget expenditure related to state aid control will therefore increase.

Government procurement

Benefits

There have been positive institutional shifts with regard to the progressive implementation of EU legislation standards in the field of government procurement. This is in the context of signing the economic part of the Association Agreement, and the prospects of the country joining the EU member states. They include the new edition of the Law of Ukraine "On government procurement" that has been recently adopted by the Verkhovna Rada of Ukraine. It stipulates: for more than fourfold reduction of the number of cases not covered by the Law; introduces the new concept of procurement customers according to the principles of the EU Directives; reduces the list of reasons for use of non-competitive procurement procedures; prohibits affiliates and offshore entities to take part in procurement; as well as a number of other standards to enhance the competition among bidders.

Taking into account the content of certain provisions of Chapter 8, "Government procurement" of section IV of the Agreement, it should be noted that implementation of the relevant EU Directives into national legal framework should take into account the multiplicity of Ukrainian legislation on government procurement and specifics of implementation of European regulations in this area. The legal mechanism of the EU Directives must be used for the application by Ukraine of a number of caveats and exceptions to the European legislation on government procurement with respect to both the conventional sector and municipal services. This will ensure the interests of Ukraine and its economic security.

It is expected that the activity towards the implementation of requirements of the Agreement will entail both positive and negative consequences for the Ukrainian economy and domestic manufacturers; but on the whole, to date there is no alternative to the country's integration into the European government procurement market.

Challenges

As a result of the opening of the state procurement market, the trend for support of foreign entities out of public funds (provision of markets for foreign entities instead of support of domestic producers) should be expected. This is because, at the time of procurement, in most cases they will be more competitive compared to domestic ones.

If the domestic economic entities will obtain access to the government procurement markets of the EU, they will face difficulties due to: their lack of experience in international tenders; lack of knowledge of the EU legislation and jurisprudence; and language barriers (English is not the official language for all EU countries, and customers in each individual country can make calls for bids or require submission of proposals in their national language).

Rural development

Benefits

Although the consequences of signing the Association Agreement for rural development in the short term will be ambiguous, in the long term they will be certainly positive.

The prospects of rural development in Ukraine are associated with taking advantage of the opportunity to introduce institutional models and mechanisms (or elements thereof) approved in the EU into the domestic rural development practice. There is also the possibility of attracting funds of CAP (Common Agricultural Policy) of the EU to solve the issues of rural development in Ukraine.

Challenges

A number of provisions of the Association Agreement with the European Union are indirectly related to the rural sector of the society. They will induce corresponding changes in government regulation of this sector in Ukraine. In particular, financial support for adaptation of peasant commercial farms to modern sanitary, veterinary and phytosanitary requirements in the production of agricultural products is estimated at 500 million UAH.

Approaches to reduction of risk of the FTA with the EU for Ukraine's economy

The warnings must be taken into account on the possible negative consequences for Ukraine's economy of implementing the Agreement. This will reduce the degree of risk associated with the implementation of its provisions.

For this purpose, it is necessary to encourage enterprises to develop and implement investment programs with the purpose of achieving the modern technology level. If domestic mechanical engineering, metallurgy and chemical industry producers fail to take effective measures to modernize production facilities, then the disparities in technology structure of production output will aggravate. The result will be further losses of internal and external markets.

Without modernization of production facilities and inclusion of Ukrainian enterprises into the processing chain of European companies, it is impossible to overcome the negative consequences of breaking the cooperative relations with Russian enterprises. The adverse effects may be partially offset by deeper cooperation with the EU through the involvement of Ukrainian economic entities in general research, communication and information projects (as provided by the Agreement section IV "Trade and Trade Related Issues" and V "Economic and Sectoral Cooperation").

An important task is the geographical diversification of exports for the companies that are losing markets in the CU/SES countries. To achieve this, in most cases, they also need to modernize their production facilities.

It is necessary to create new jobs for the workers of the enterprises losing their jobs as a result of the loss of markets in the CU/SES countries. Their employment can be achieved through promotion of foreign direct investment to Ukraine, and improvement of the business environment for small and medium-sized businesses. It is important to draw on EU financial assistance for solving these problems.

To reduce the risks of the FTA with the EU, it is important to strengthen the role of industry associations, and deepen cooperation between government and business, taking into account the experience of the EU countries.

The possibilities of integration into the European trade area can be implemented only subject to improvement of the institutional environment in the field of technical regulation, and compliance with sanitary, phytosanitary, environmental requirements, etc. Implementation of the relevant legislation within the period of 2-3-5-7 years, stipulated by the Association Agreement with the EU, is onerous. It will also require significant accumulation of funds for technology upgrades. In accordance with Article 57 of the Agreement, "Convergence of Technical Regulations, Standards and Conformity Assessment", the implementation schedule may be revised with Ukraine defining the new implementation schedule independently. It is therefore necessary to negotiate with business representatives on coordination of rescheduling of implementation of the provisions of the Agreement in the technical field to prepare for negotiations with the EU.

To reduce the risks associated with abolition of product names, which coincide with the EU geographical designations, the Agreement contains the possibility of the use of the EU compensation package. It is also important to involve EU technical and financial assistance to promote products with new names in the market, which is also stipulated in the Agreement.

Effective implementation of the provisions of the Agreement, and the reduction of related risks, is not possible without the use of institutional capacities. These are provided in the Agreement on coordination of implementation of its provisions. In accordance with Article 466, the Association Council (the creation of which is stipulated by the Agreement) may decide to set up other special committees or bodies in specific areas that will be formed by the representatives of the governments of Ukraine and the EU. For example, within the framework of the FTA with the EU, the creation of the Committee on Trade is stipulated, with a number of subcommittees, including the Subcommittee on Management of Sanitary and Phytosanitary measures (SPM). It will regularly monitor implementation of the process of convergence between Ukrainian and European legislation, with a view to preparing recommendations on convergence measures (Art. 74). To maintain the position of Ukraine in committees and subcommittees established within the framework of the Association, it is necessary to actively involve the industry associations. The pre-accession support package of Ukraine, approved by the European Commission on March 5, 2014 is aimed at financial support of implementation of the provisions of the Agreement, amounting to 11 billion Euros, of which 5 billion Euros will come from the European Bank for Reconstruction and Development[2]. Amounts of support for Ukraine are comparable to the amount of support for countries that were candidate for accession to the EU. It is known that Poland received the largest pre-accession financial support from the EU: according to the Committee for European Integration of Poland during 1990-2003 the estimated amount of support for Poland's accession to the EU was 5.7 billion Euros. The support package of Ukraine will be partly aimed at supporting political and economic reforms, including those that are defined in the Association Agreement and deep and comprehensive FTA with the EU. The economic support will be provided in the form of macro-financial assistance (loans amounting to 1.6 billion Euros[3]) and development support package in the form of grants in the amount of 1.4 billion Euros, which will be available over the period of seven years.

[2] European Commission's support to Ukraine. EuropeanCommission [Electronic resource]. — MEMO/14/159 05/03/2014. — Access mode : <http://europa.eu/rapid/press-release_MEMO-14-159_en.htm>.

[3] Pre-accession funds. Polish experiences [Electronic resource] / Office of the Committee for European Integration. — Warszawa — Access mode: <http://archiwum-ukie.polskawue.gov.pl/HLP/files.nsf/0/8A25581477E1ED88C1256FE10047F1A9/$file/Pre-accesion_funds_Polish_experiences-publikacja.pdf>.