



UKRAINE AND THE WTO: HOW TO MAKE THE PLUSES LARGER AND THE MINUSES SMALLER

The issue of entering the World Trade Organization is high on Ukraine's agenda. Its non-participation in this global economic organization has no reasonable explanation: in late 2001 the WTO was joined by China, prospects for Russia becoming its member in 2003 have become more or less definite. The beginning of a new round of multilateral trade negotiations in the WTO frameworks will obviously raise the global economic regulation system to a new level and will lead to a considerable influence on Ukraine. After all, joining the WTO is a prerequisite for Ukraine's real, not simply declarative, integration with the European Union.

On July 3, a round table was organized in Kyiv by the Razumkov Center and the Kyiv office of the Eurasia Foundation to discuss Ukraine's relations with the WTO and assess the conditions and likely effects of joining it. The discussion involved about 150 representatives of government bodies, foreign embassies, staffers with the National Science academy, experts with non-governmental research organizations, and representatives of the mass media.

The new prospects for the WTO are defined in the Declaration of the 4th Ministerial Conference in Doha, Qatar. The Declaration provides for holding of talks before January 1, 2005 on a wide range of issues which would stimulate the development of international economic regulation mechanisms, extend the sphere of their influence and increase their effect on all national economies. It is extremely important for Ukraine to take part in such talks, in order to maintain its national interests. However, the new round of talks has complicated the task of adapting to the parameters of the multilateral trade system and under these conditions Ukraine cannot count on easy terms of acquiring membership.

Other countries' experience of negotiating WTO membership shows that concrete terms of joining it may undergo significant changes, depending on the level of the negotiators' professionalism and political will. That is why the agreements on joining the WTO differ so greatly: for instance, countries whose macro-economic performance is better and whose level of development is higher are given consent to set higher import tariffs.

If any negotiations take less time, it is not necessarily due to the effectiveness of the negotiation process. The reason could be that the candidate country wants membership at any cost, including quick surrender of its positions. And lengthy negotiations may result either from a principled position or from weak reforms, or from an inability to negotiate consistently and purposely. In Ukraine's case, we have seen all these factors at different stages of the negotiation process.

The key question in the context of joining the WTO is: how to maximize the potential advantages of being part of the multilateral trade system, and how to minimize any possible negative consequences of entering it?

Possible Consequences of Joining the WTO

The possible consequences of joining the WTO have found no systematized analysis in this country. Unlike in Russia, there has been no tender for an independent study of this problem. The government has not consulted Ukrainian businessmen on tentative terms of joining the WTO. It has not invited any experts. In Russia, during 2001, the Ministry of Economic Development and Trade had more than 260 meetings with unions or associations of producers to discuss Russia's positions at the negotiations of joining the WTO.

This certainly tells negatively on the Ukrainian government's ability to objectively evaluate the numerous positive and negative factors of the influence of its prospective membership in the WTO on its economic and social sectors.

In theory, joining the WTO could give Ukraine many new opportunities.

Ukrainian producers ought to gain from a wider choice, higher quality and lower prices of goods and services as a result of more effective competition. Prices would go down not only for finished imported goods and services, but also for domestic ones, where imported components are used. Also, there would be subsequent changes in the volume and structure of consumption which would approximate the standards of the developed economies. An increased solvent demand would have a positive effect on production growth and improvements in people's social and economic status.

Producers could gain from easier access to the world markets of goods, services and capital, from internationally recognized rights to protect the national interests in these markets. Commercial risks would be lower due to the establishment of a more stable trade regime and transport expenses would be lower due to a guaranteed free transit of goods within the WTO territory. As a result, the cost of Ukrainian products would be lower and the competitiveness of Ukrainian companies would grow.

The export-oriented industries could sustain smaller losses from discriminative measures (which currently amount to \$2 billion - \$3 billion annually), particularly, anti-dumping investigations. This country could have more possibilities to defend its national interests thanks to the multilateral mechanisms of a just resolution of trade disputes which are applied within the WTO.

There is one more potential advantage - Ukraine may be internationally authorized to defend its own market and industries in accordance with the GATT Article 12 on the limitations on keeping the stable payment balance; with the agreements on protective measures, on agriculture, on application of sanitary measures, on subsidies and compensations; with GATT Article 6 on anti-dumping and compensatory measures.

It is important, however, that these positive effects should be tied to additional incentives for reforms within the country. Within a civilized environment of competition and a transparent legal field, structural reforms could gain momentum, competition and innovations could receive fresh impetus. This would be facilitated by the adjustment of the national legislation (on taxation, customs, standardization and certification, services, competition, intellectual property) to the WTO standards and rules. With the government's policy becoming more transparent and a great number of preferences abolished, trade would become free from administrative pressure. Also, it would no longer be necessary to lobby excessively corporate interests in parliament. And this is an important prerequisite for a more effective struggle against corruption.

But the practical experience of many WTO member-nations, especially developing ones, proves that most of the possible positive effects for the country and its industries do not come automatically. They are achieved by a rational policy which creates the potential for using such opportunities. That is why one of the terms used in the WTO today is "capacity building" - the creation of a potential for using the available opportunities.

How to Make the Best of WTO Membership?

In order to make the best of membership in the WTO, we should be aware of its limitations.

The advantages of free access to the market provide by WTO membership mostly concern markets with predominantly price competition, i.e. markets of raw materials and standard ready-made consumer products. To a much lesser degree they concern hi-tech products circulating within the closed turnover of transnational companies which are less influenced by liberalizing the measures of the WTO. Therefore, if Ukraine relies on trade liberalization only, it is doomed to remain for a long time in the low-profit niche of low-tech export, which will further deter domestic reforms. This nation has to use a wider arsenal of economic policies which would speed up innovations in potentially competitive sectors, and create favorable environments for forming powerful and globally competitive transnational companies in Ukraine.

The possibility of increasing the volume of sales of Ukrainian goods and services to foreign markets may be prevented by the incompatibility of Ukraine's commodity export structure with international. In 2001, Ukrainian exports were dominated by non-precious metals (41.3%), agricultural products (ca. 11%), chemicals (ca. 9%), textiles (3.8%). The products of machine-building and instrument-making, means of transport accounted for a mere 14.3%. The situation on the world commodity market is entirely different. According to the WTO International Trade Statistics 2001, during 1990-2000 the share of ferrous metals decreased from 3.1% to 2.3% (down to \$144 billion), textiles - from 3.1% to 2.5% (down to \$157 billion), agricultural products - from 9.3% to 7.2% (down to \$558 billion). At the same time, the share of office and telecommunications equipment increased from 8.8% to 15.2% (up to \$940 billion). The same can be said about Ukrainian exports of services which were dominated in 2001 by transport services (83.5%), while in world exports they stood under 23%. Also, export of tourist services in Ukraine makes up 2.3% of the total, while the figure for world exports is 23%.

So without a structural adaptation to the priorities of a global economy, without developing adequate innovative and investment strategies, Ukraine can forget about the advantages of the global trade system.

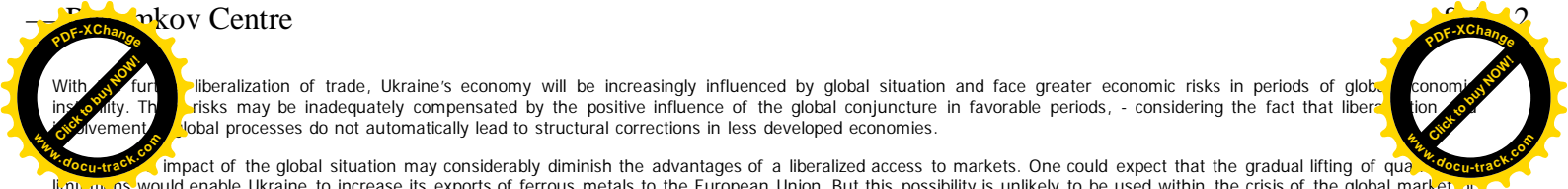
One should not expect Ukraine's membership of the WTO to remove the threat of anti-dumping investigations, although it strengthens the position of any country that is under such an investigation. The number of anti-dumping measures against WTO member-nations is growing. According to the WTO Secretariat, during 1995-2001, 1845 anti-dumping investigations were launched, 1066 cases of the imposition of anti-dumping customs duties were registered. Notably, in 2001 the number of such cases grew to 330 as compared to 1995 from 157 and from 118 to 163 respectively.

An effective use of the WTO mechanism of multilateral settlement of disputes may be deterred by the fact that the Ukrainian economic sectors lack experienced specialists in international trade law. With such a shortage, Ukraine will have a difficulty in using the advantages of its membership in the WTO and in avoiding unjustified expenses in the process of entering it.

How to Minimize the Possible Negative Effects of Joining the WTO?

Joining the WTO may aggravate a number of internal economic problems in Ukraine which are less marked at present, due to certain trade barriers and the government's supportive measures for certain industries. The possible negative effects are as follows.

With the further liberalization of trade, Ukraine's economy will be increasingly influenced by global situation and face greater economic risks in periods of global economic



liberalization of trade, Ukraine's economy will be increasingly influenced by global situation and face greater economic risks in periods of global economic crisis. These risks may be inadequately compensated by the positive influence of the global conjuncture in favorable periods, - considering the fact that liberalization of trade processes do not automatically lead to structural corrections in less developed economies.

The impact of the global situation may considerably diminish the advantages of a liberalized access to markets. One could expect that the gradual lifting of quantitative restrictions would enable Ukraine to increase its exports of ferrous metals to the European Union. But this possibility is unlikely to be used within the crisis of the global market for ferrous metals and subsequently coordinated reductions in European capacities in this sector.

Concentrating on potential long-term advantages of its membership of the WTO, Ukraine may underestimate some of the effects of the initial period. The government may fail to come up with adequate measures under unfavorable circumstances (it is quite possible, especially with the inadequate approach to formulating conditions and defending the national interests in the process of joining the WTO).

There may be some complications within the sphere of state regulation of economic development caused by: a) shifting to new, internationally agreed terms of state regulation of economy and b) giving up the traditional vertical levers of economic policy. The latter concerns possibilities to use tax and other privileges, to write off companies' debts to the state, to use state purchase orders as an instrument to stimulate domestic producers, to control and regulate financial flows, to tell foreign investors where they should buy raw materials and manufactured parts and where they can sell their goods. Ukraine would have to cancel many privileges which are presently enjoyed by the national coal-mining, metallurgy, ship-building, automobile- and aircraft-making industries but which are incompatible with WTO rules. Although these changes can be regarded as a positive factor within a long-term context, within a short-term context they could cause problems for these sectors. There may also be complications for the producers that work under the system of state purchase order, without open competition.

One of the most serious of the negative factors activated by WTO membership is that some Ukrainian producers may find themselves unprepared for the tough international competition. Ukraine's competitiveness potential is still low by international standards. According to the Global Competitiveness Report 2001-2002 drawn by the World Economic Forum, in 2001 Ukraine's competitiveness rating was only 69th out of 75 countries.

The returns of a poll among 83 Ukrainian and foreign experts conducted by the Razumkov Center from May 28 to June 14, 2002 show serious doubts about the chances of many national producers to withstand future competition. No other potential problem listed in the questionnaire collected as many votes than "the aggravation of problems connected with low competitiveness of industries, dwindling production, growing unemployment": this point was marked by 58.5% of respondents in relation to a period of less than one year after joining the WTO, 59.8% - a period up to five years and 30.5% - a period exceeding five years.

However, there are no sufficient grounds to expect a completely negative impact, although there have been apocalyptic forecasts of the ruin of Ukraine's economy after it joins the WTO. In reality, the national commodity market is unlikely to be damaged.

According to the data of the Ministry of Economics and European Integration, the level of tariff security of the domestic market already equals that of the countries which joined the WTO after 1995, with 80% of Ukrainian customs duty rates standing at the level of the new members (Albania, China, Croatia, Estonia, Latvia, Lithuania, Moldova, Taiwan), about 7% of duty rates being under this level and only 13% of duty rates exceeding it. Moreover, the Ukraine-Europe Consultative Center estimates that real added customs tariffs will be in Ukraine at 1% - 2%. This means that already even before Ukraine joins the WTO, they are lower than in the EU, the USA or Japan. This figure is so low because the majority of Ukrainian importers of consumer goods evade customs duties. So the level of tariff security is very unlikely to be reduced substantially when Ukraine joins the WTO, considering the fact that the WTO rules and standards involving customs valuation procedures and abolition of privileges to specific industries are aimed at the opposite - higher customs duties.

These arguments and the expert opinions make us believe that the diverse impact of joining the WTO will reflect on different sectors of the national economy. However, the negative influence will tend to recede, as is forecast by the experts whose pessimism about the long-term period is almost twice as small.

The Likely Consequences of Joining the WTO for Ukraine's Economic Sectors

High probability of prevailing positive consequences

Food industry, light industry, telecommunications, tourist services, stock markets, pipelines, insurance, postal services, banking services.

Certain probability of prevailing positive consequences

Aircraft-building, ship-building, chemical industry, agriculture, railroad transport, realty services, education, marine transport, medical services.

Possible balance between positive and negative consequences

Power engineering, aviation transport.

Certain probability of prevailing negative consequences

Metallurgy.

High probability of prevailing negative consequences

Automobile-making, coal-mining, radio-electronic industry, agricultural machine-building.

The Ukrainian agricultural sector is also likely to face the problems of drastic restructuring, as it presently enjoys protection from external competition.

On the other hand, the level of state support to domestic agricultural producers is much lower than in the developed economies. In recent years, the government has spent about 0.5% of GDP on this, whereas Hungary has spent 1.8%, Japan and the EU countries - 1.7%, the Czech republic - 1.6%, the USA - 1.5%, Canada - 1.3%, Russia - 0.8%. Per capita subsidies total \$566 in Japan, \$355 in the USA, \$336 in the EU, \$163 in Canada, \$111 in Hungary, \$100 in the Czech Republic, \$60 in Russia and only \$3.3 in Ukraine.

But here, too, Ukraine may face problems when the subsidies are cut that are liable to prohibition or limitation under the Agreement on Agriculture and subsequent raising of permitted subsidies - for funding research, educational, consultative and marketing programs, state reserves to ensure food security, insurance and security of incomes, damage compensations, structural reformations, environmental programs and regional aid programs.

Problems of restructuring are also likely to have to be faced within the Ukrainian service sector. WTO candidate countries are required to have a more rigid approach to obligations in the service sectors. This applies to both the scope of obligations and restrictions for the application of interim provisions in the period of their introduction. It should be noted, however, that most sectors of services are less vulnerable to international competition than those engaged in the manufacture of commodities. Because local providers of services have advantages before foreign ones thanks to their better understanding of local customers and local traditions, legislative and administrative regulations, closer public relations and to the absence of a language barrier.

There is an exception: the sector of air and, partly, sea transportation, where accelerated liberalization and non-application of preventive measures in an effort to raise the competitiveness of national carriers may lead to their partial exclusion from international transportation markets.

Ukraine has a certain margin of safety: its foreign trade balance is positive; the share of imports of foods and nonfoods, the foreign debt and the spending on its servicing, the share of oil import from one supplier country in the total amount, the import-export ratio are at a safe level. So joining the WTO should not affect Ukraine's economic security. But its gold reserves are still insufficient to guarantee macro-economic stability under any increased influence on its economy from global fluctuations. As for the growing share of hi-tech and machine-building products, it will largely depend on the ability of the national industry to adapt to tougher competition and shorter terms set for innovations.

In appraising possible problems and risks ensuing from membership of the World Trade Organization, one should not generalize them. It is possible in principle to take measures to prevent or minimize them. Such measures should be included in final Ukraine-WTO agreements and in the government's program of actions for joining the WTO.

On the whole, joining the WTO meets Ukraine's strategic interests. It would mean a sharp turn from the practice of arbitrary introduction and application of rules of economic conduct to a gradual introduction of internationally recognized rules. This step may become decisive in the process of building a civilized market economy, carrying out radical administrative and structural reforms, accelerating Ukraine's integration with global and European economic and political structures.

The problems emerging during this route should not be regarded as reasons to delay this process. On the contrary, they demand an acceleration of social and economic transformations on the basis of clearly formulated objectives tied closely to Ukraine's international obligations. To wait for the day when this economy becomes competitive enough to be ready to be a member of the World Trade Organization - as is proposed by those who criticize Ukraine's membership bid - is about the same as to hope to learn to swim without stepping into the water.

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