

EUROPEAN PARLIAMENT



session documents

ENGLISH EDITION

2 December 1994

A4-0094/94

REPORT

on economic and trade relations between the European Union
and the Ukraine

Committee on External Economic Relations

Rapporteur: Mrs Erika Mann

DOC_EN\RR\261\261864

PE 210.069/fin.
de - Or. de

- * Consultation procedure
simple majority
- **I Cooperation procedure (first reading)
simple majority
- **II Cooperation procedure (second reading)
simple majority to approve the common position
absolute majority of Parliament's component Members to reject or amend the common position
- *** Assent procedure
absolute majority of Parliament's component Members to give assent
except for simple majority under Articles 8a, 105, 106, 130d and 228 EC

- ***I Codecision procedure (first reading)
simple majority
- ***II Codecision procedure (second reading)
simple majority to approve the common position
absolute majority of Parliament's component Members either to adopt a declaration of intent
to reject the common position, or to amend or confirm the rejection of the common position
- ***III Codecision procedure (third reading)
simple majority to approve the joint text
absolute majority of Parliament's component Members to reject the Council text

DA

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At the sitting of 30 November 1994 the President of the European Parliament announced that, pursuant to Rule 148 of the Rules of Procedure, the Conference of Presidents had authorized the Committee on External Economic Relations to draw up a report on economic and trade relations between the European Union and the Ukraine.

At its meeting of 4 November 1994 the Committee on External Economic Relations had decided to draw up a report and appointed Mrs Mann rapporteur.

It considered the draft report at its meeting of 29 November 1994.

At this meeting it adopted the motion for a resolution unanimously.

The following took part in the vote: De Clercq, chairman; Pex, vice-chairman; E. Mann, rapporteur; Arroni (for Malerba), Dimitrakopoulos (for Valdivielso de Cué), Ferrer, Imbeni, Kittelmann, Kreissl-Dörfler, Miranda de Lage, Moniz, Sonneveld (for Schwaiger), Van der Waal (for Goldsmith) and Wiersma (for Falconer).

The report was tabled on 2 December 1994.

The deadline for tabling amendments will appear on the draft agenda for the part-session at which the report is to be considered.

A
MOTION FOR A RESOLUTION

Resolution on economic and trade relations between the European Union and the Ukraine

The European Parliament,

- having regard to its resolution of 9 July 1992 on economic cooperation between the European Community and the Commonwealth of Independent States¹,
 - having regard to its resolutions of 12 March 1993 on future agreements between the Community and the New Independent States of the former Soviet Union² and of 21 April 1994 on the situation in the Ukraine³,
 - having regard to the agreement on partnership and cooperation negotiated between the European Union and the Ukraine and the interim agreement under which the trade provisions of the partnership agreement between the European Union and the Ukraine are scheduled to enter into force beforehand,
 - having regard to its endorsement of the partnership agreement,
 - having regard to Rule 148 of its Rules of Procedure,
 - having regard to the report of its Committee on External Economic Relations (A4-0000/94),
- A. whereas economic and trade relations with the Ukraine are still based on the trade and cooperation agreement concluded in 1989 between the European Community and the former USSR,
- B. whereas, following the collapse of the USSR, the Ukraine as an independent state controls part of the nuclear potential of the former USSR,
- C. whereas the Ukrainian Parliament has approved the Ukraine's accession to the Non-Proliferation Treaty (NPT),
- D. whereas the Ukraine had so far hardly begun to make adequate efforts to turn its economic system into a free and social market economy,
- E. having regard to the encouraging inaugural speech by Mr Kutchma, the newly-elected President of the Ukraine, in which he set out plans for comprehensive political and economic reforms,
- F. having regard to the technical and financial aid granted to the Ukraine by the European Union and its Member States and the other western industrialized nations,

¹ OJ C 241, 21.9.1992, p. 161

² OJ C 115, 26.4.1993, p. 248

³ OJ C 128, 9.5.1994, p. 309

1. Welcomes the conclusion of the partnership and cooperation agreement and its ratification by the Ukraine on 10 November 1994 and calls on the Member States to ratify this agreement forthwith so that the wide-ranging cooperation provided for in the agreement can begin as soon as possible;
2. Notes that the partnership agreement is more than a mere trade and cooperation agreement since by establishing a political dialogue and cooperation in the fields of internal security, it covers all areas of Union policy, as redefined in the Treaty on European Union;
3. Stresses that respect for democratic principles and human rights is not only the basis for mutual cooperation but is also an essential precondition for the success of market economic reforms;
4. Is concerned at the present economic situation in the Ukraine which is characterized by an even sharper decline in productivity and greater imbalances in the economy as a whole than the other CIS Republics, for example;
5. Attributes these developments primarily to the excessive budgetary deficit of the Ukraine and the fact that central bank loans are used to fill this deficit;
6. Points out that, in order to overcome this economic crisis, a national consensus is necessary to allow the burden of adjustment to be divided equally among all sectors of the population;
7. Welcomes the recent agreement concluded between the Ukraine and the International Monetary Fund (IMF) on the granting of \$ 371 million to help the balance of payments as part of the Systemic Transformation Facility, under which the Ukraine has pledged, on the basis of respect for democracy and human rights, energetically to endeavour to stabilize the economy as a whole by reducing its macroeconomic imbalances;
8. Is aware that, given the overall economic conditions, a lending commitment by the EU is very risky, but nevertheless calls on the Council forthwith to approve the Commission's proposal to grant the Ukraine balance of payments aid amounting to ECU 85 m since, without a financial contribution by the EU, aid for other donor states and international financial institutions is blocked;
9. Calls on the Commission to forward this proposal to it immediately, so it can deliver an opinion on it;
10. Welcomes the fact that the partnership agreement provides for closer economic cooperation between the Ukraine and the other CIS Republics, as part of which traditional supply networks in the field of energy and raw materials and agricultural products could be reactivated;
11. Draws attention to the problems the Ukraine still has to contend with in repairing the damage caused by the Chernobyl nuclear disaster and ensuring energy supplies;
12. Welcomes the decisions taken by the European Union and the other industrialized nations concerning aid to the Ukraine aid to tackle these problems;

13. Draws attention to the importance of the agricultural market for the Ukraine which is a major agricultural producer; calls, therefore, on the Commission to consider to what extent it can help the Ukraine by granting it additional trade concessions in the agricultural sector as part of the partnership agreement, while ensuring that this does not disrupt the Union;
14. Hopes that the forthcoming and current negotiations on specific additional agreements concerning trade in textiles and steel products will soon be brought to a successful conclusion and that trade in nuclear materials can also be governed by an agreement of this kind;
15. Calls on the European Union and the Member States to increase cooperation in the areas of research, development, technology transfer and industry and in the cultural sphere;
16. Highlights the importance of the approximation of legislation agreed on in the partnership agreement and the commitments undertaken in the field of competition law, the protection of intellectual property and public subsidies which are designed to establish an equitable basis for the reciprocal exchange of goods;
17. Considers that until these provisions are fully implemented the European Union must be able to resort to trade protection measures in cases where the market is being disrupted, for example by dumped or subsidized imports from the Ukraine, although this facility must not be misused for protectionist purposes;
18. Is aware that, if the Ukraine joins the WTO, the partnership agreement provisions on the traffic in goods, transfrontier service transactions and the conditions of establishment will have to be revised and, if this occurs, looks to the Ukrainian side to improve market access and working and establishment conditions for EU undertakings;
19. Is concerned that, contrary to the provisions of the partnership agreement, the Ukraine's rules on establishment discriminate against maritime transport undertakings from the EU and hopes that both sides will rapidly reach an agreement so as to prevent any further delay in the conclusion of the partnership and interim agreement;
20. Instructs its President to forward this resolution to the Commission, the Council and the governments of the Member States and the Ukraine.

B
EXPLANATORY STATEMENT

I. THE ECONOMIC SITUATION IN THE UKRAINE SINCE INDEPENDENCE

1. With 52 million inhabitants, the Ukraine, which became independent in August 1991, is the most important successor state to the former Soviet Union after Russia. It could become an important political and economic partner of the European Union in the future. Its people are well educated, its agricultural land is extremely fertile, its extensive heavy industry includes oil refineries, coal, steel and shipbuilding, and it is the transit country for Russian oil and gas supplies to Western Europe. The armaments sector accounts for over 30% of Ukrainian industrial production. The Ukraine still has nuclear weapons, and its army of half a million men is the second largest in Europe after Russia's. It recently advocated the renunciation of nuclear weapons and expressed its willingness to accede to the Non-Proliferation Treaty.

2. Despite or, in some ways, precisely because of these factors, the process of restructuring from planned to market economy in the Ukraine is proving to be far more problematical than in its larger neighbour, Russia. Since independence the macroeconomic situation has steadily deteriorated. The main cause so far has been the absence of any political support for a strategy for coping with the dissolution of past economic structures and the severing of links with the countries of the former USSR.

3. On the other hand, it must be realized that the Ukraine became an independent state under extremely difficult circumstances. Despite the legacy of important industrial sectors (in 1989, for example, the Ukraine produced 34% of the Soviet Union's steel, 46% of its iron ore, 36% of its television sets and 53% of its sugar), the break in trade relations with Russia and the other successor states to the USSR meant the loss of a fifth of its export market. Other burdens stem from the costs following the Chernobyl disaster, the maintenance and reduction of the armed forces, nuclear disarmament and the conversion of the military industrial complex.

4. At the same time, the Ukraine had to continue importing energy from Russia at a price that was gradually being adjusted to the world market level. This led to higher prices and major payment difficulties for the Ukraine's still state-owned and obsolete industry. In the absence of a functioning capital market, the Ukrainian Government reacted with excessive tax increases and an increase in the money supply by printing money. As a result, domestic enterprises sought refuge in the black-market economy, and the money supply and inflation exploded.

5. Since the state was founded, the gross national product has fallen by 35%. Inflation is said to have reached over 10 000% at times in 1993, and although it has dropped significantly, it remains high in 1994, at 6% per month. The value of the Karbovanets in the free market continues to fall, even against the rouble. Although unemployment is officially below 1%, unpaid wages and compulsory leave are causing considerable hardship. At US\$ 9 to 10, the average income of a Ukrainian is about a tenth of a Russian's. On the other hand, the official statistics say little about the not inconsiderable growth of the private black-market economy that is developing while the official economy declines. In general, the decline of the Ukrainian economy is slowing visibly, and the time has now come for an economic and political signal to bring about an upturn.

Economic data on the Ukraine, 1992 and 1993

| | | |
|----------------------------|-------|--------|
| GNP growth rate | - 17% | - 14% |
| Public sector share of GNP | 44.0% | 54.8% |
| Exchange rate against US\$ | | |
| - official | 638 | 5 970 |
| - unofficial | 1 050 | 31 000 |
| Trade deficit (in US\$ m) | 1 210 | 4 735 |

(Sources: IMF and US Embassy, Brussels)

6. The Ukraine is currently having to contend with a serious balance-of-payments deficit estimated at US\$ 1.8 billion, which - together with an external debt officially estimated at US\$ 7.8 billion - threatens to stifle any reform and attempts at economic stabilization unless substantial western support is forthcoming. The deficit is mainly due to the rise to the world market level of the prices of the Russian and Turkmen energy imports that meet 90% of the Ukraine's requirements.

II. THE UKRAINE'S RELATIONS WITH THE EUROPEAN UNION

7. Any improvement in relations with the Ukraine has been largely hampered in the past by the lack of reforms in the country. The European Union's policy is to promote democratic and economic development in the Ukraine by supporting its independence and territorial integrity, by providing technical assistance (TACIS) and implementing bilateral aid programmes, by guaranteeing credits for food and medical supplies and by taking wide-ranging measures relating to nuclear safety and the restructuring of the energy sector.

8. In October 1992 the European Union and the Ukraine began negotiating a partnership and cooperation agreement, which was signed on 14 June 1994. It is the first agreement of this kind to be concluded with one of the successor states to the USSR, and it creates a framework for both economic and political cooperation. A Parliamentary Cooperation Committee is to deepen the political dialogue, which extends to all the European Union's areas of activity, including the various aspects of internal security. Provision is made for far-reaching liberalization of trade in goods, investment, services, payments and capital movements. The protection of intellectual property and cooperation in research and technological development and in the civil use of nuclear power are also improved.

9. One of the most important aspects of the partnership and cooperation agreement will be the mutual granting of most-favoured-nation treatment. This will make for trading conditions comparable with those of the GATT. Even more important, however, is the prospect of the establishment of a free trade area. This will, however, depend on a review planned for 1998 of the Ukraine's progress in developing a market economy. It is estimated that a free trade area of this kind might lead to a fourfold increase in trade in goods between the two trading partners.

10. As the partnership and cooperation agreement is a 'mixed agreement' (falling under national and Community terms of reference), the ratification procedure is bound to take a very long time. To enable the Ukraine to enjoy the trade advantages of the agreement as soon as possible, an additional, interim agreement for which the Union alone is responsible and which anticipates the

trade aspects of the partnership and cooperation agreement was concluded. It will enter into force in all probability on 1 January 1995 and is dominated by the principles that most-favoured-nation treatment should apply as far as possible and that quantitative restrictions should be removed. The Ukraine has also applied for membership of GATT and intends to become a member of the WTO.

11. Both the partnership and cooperation agreement and the technical assistance provided under the TACIS programme (amounting to some ECU 120 million from 1991 to 1994) are designed for the long term, the aim being to help the Ukraine with its structural adjustment process. It would be appropriate in this context if TACIS also placed some emphasis on technical assistance in foreign trade and the penetration of western markets and on mobilizing the know-how that exists in the Ukraine.

12. The political and economic problems facing the country are, however, so serious that long-term assistance alone is not enough. The European Union must provide the Ukraine with additional short-term aid to bring about rapid improvements. Accordingly, the European Council meeting in Corfu in June 1994 instructed the Council to formulate an all-embracing EU policy towards the Ukraine. In October the Council of Foreign Ministers approved a strategy paper geared to

- (a) establishing close political relations to prevent the Ukraine from coming under Russian influence;
- (b) safeguarding democratic development;
- (c) ensuring the early fulfilment of the Ukraine's commitment to nuclear disarmament and accession to the Non-Proliferation Treaty;
- (d) implementing the global programme of stabilization and economic reform agreed by the Ukraine and the IMF;
- (e) integrating the Ukraine into the world economy and promoting trade, investment and economic cooperation with the EU;
- (f) implementing the G7's plan of action for the closure of Chernobyl, which has been approved by the Ukraine.

III. THE UKRAINE'S REFORM PROGRAMME AND WESTERN FINANCIAL AID

13. None of this can, however, be properly achieved unless the Ukraine is prepared to make comprehensive efforts of its own. Reforms and support measures must go hand in hand. Since last summer's elections the Ukraine has shown that it is willing to chart a new economic course. President Kutchma, the promoter of this process, wants to lead the Ukraine out of its isolation. The country has reached agreement with the International Monetary Fund on a tough reform programme with clearly defined objectives:

- the liberalization of prices, exchange rates and trade;
- a restriction of the decline in GNP and a drastic reduction in the rate of inflation;
- a reduction in the budget deficit through cuts in public spending and short-term deferments of external debt repayments;
- a reduction in the trade deficit;

- the development of an efficient market economy through accelerated privatization, land reform and elimination of monopolies, the promotion of the establishment of small and medium-sized enterprises;
- deliberate social cushioning of the economic reforms to help the poorest sections of the population.

14. The agreement with the IMF provides for a Systemic Transformation Facility (STF), whereby the Ukraine is to receive a first tranche of US\$ 371 million in 1994 for its structural adjustment process. A further tranche may follow in 1995 in the form of a standby credit. These resources are, however, linked to a substantial commitment by the western industrialized countries. The USA (the Ukraine being the fourth largest recipient of US financial aid), Japan and Canada have already given appropriate assurances, and the Commission has also submitted to the Council a proposal for ECU 85 million in macro-financial aid to the Ukraine. Regrettably, no agreement on this has yet been reached in the Council, which is very disturbing. A Council decision against the EU contribution will cast doubt on the whole western credit package and thus on the success of the Ukraine's economic reforms. Yet, as the Council itself has emphasized in its global strategy for the Ukraine, this country's destiny is extremely important for the security of the European Union and of the Central and Eastern European countries.