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## PROSPECTS AND CHALLENGES OF RESTRUCTURING TRANSACTION SECTOR UNDER THE EFFECT OF THE EU-UKRAINE ASSOCIATION AGREEMENT

**Summary:** In article the main challenges and influence of transaction policy on transaction sector is analyzed. The term international transaction sector is introduced. The consequences for various international transactions and almost all transaction processes in Ukraine, caused by signing of EU-Ukraine Association Agreement, are investigate.

**Keywords:** domestic transaction sector, international transaction sector, EU-Ukraine Association Agreement.

### Introduction

Almost all transaction processes in Ukraine are changing with signing of EU-Ukraine Association Agreement and this has caused consequences for various international transactions. Retail turnover has already undergone a change – it has considerably contracted. In first half of 2015, it fell almost 25% over the last year. That affect on the general indicators of economic development and the structure of transaction sector. Thus, the Agreement will influence on the restructuring of transaction sector in whole.

There is one more problem that should be considered apart: the problem of restructuring of financial transactions. Signing of the Agreement has caused changes in the directivity of external transactions. Russia has interrupted the

credit Agreement for 15 billion dollars after providing the first three billion, but the loans from the international organizations and some Western countries have been received. In particular, at the end of July 2015 we have learned about EU macro-financial assistance for the total amount of 600 mn Euros, which can be increased by another 1,2 bn Euros, and about second tranche of 1,7 billion dollars of the IMF loan, which total size is 17,5 bn.

Signing of the Agreement has also led to deregulation of carrying out bank transactions and has accordingly changed their structure. Deposit transactions have been reduced by a third. Since the beginning of 2014, 53 banks have been removed from the market, this being the result of their non-solvency and the attempts taken for the purpose of overcoming illegal transactions. As a result, the deposit guarantee fund has been exhausted. Thus, even the brief preliminary analysis shows that practically all transactional types of economic activity turned out to have come under the influence of the Agreement.

That means is modification of the transaction sector internal structure. Changes are also likely to occur in the transaction sector in whole since the Agreement is likely to change a balance of real sector and transaction sector because of the mentioned changes in the sphere of international and domestic transactions.

For the national economy, the transaction sector restructuring is especially important in the case of losing its operating efficiency, which is taking place in Ukraine now. A major way to achieve such restructuring is to carry out the consistent government transaction policy.

The role of state in the economy under market transformation has essentially changed. In particular, it tells on the transaction activities, which is transferred from the hands of the state to the hands of the private sector and essentially changes its size and significance. However, it does not mean that the state completely abandons the transaction sphere. The state continues affecting on the transaction sector, whether voluntary or not.

Of course, it would be better if the state pursued a transaction policy especially worked out rather than taking spontaneous measures in order to regulate transaction activities, i.e. the state control is of paramount importance. The problem of government transaction policy is poorly worked out in economic literature. Following a conscious transaction policy presupposes corresponding characteristics of the transaction sector of economy. However, the problems of evolution of the transaction sector and its structure under market transformation conditions are insufficiently discussed in the existing investigations. They must deal with the problem of comprising both the transaction activities volume and transaction sector size as well as and their significance in Ukraine as an EU As-

sociated Country and different EU Member States (either core, or peripheral, or new member) economies in order to obtain the guiding line for Ukrainian government transaction policy.

An objective of the article is determining the influence of the government transaction policy is connected with signing of EU-Ukraine Association Agreement on the transaction activities and interdependence between the development of transaction activities.

## **1. Materials and methods**

The efficient government transaction policy under the Associated Agreement results in the growth of transaction sector. J. Wallis and D. North introduced the term 'transaction sector' in their well-known study. According to the approach proposed by [Wallis i North, 1986] the majority of state functions should be attributed to transaction services. At any rate, the remuneration of workers rendering such services belongs to transaction costs. They estimated the share of transaction costs in US GNP (47%-55% in 1970) and the correlation of the public and private transaction sectors on this basis.

The study of the Australian transaction sector has shown its growth up to 60% in 1991, [Dollery i Leong, 1998]. In Argentina, the transaction sector's share of GNP changed from 28% only to 35% in 1970-1980, where it remained at least to 1990 [Dagnino-Pastore i Farina, 1999].

On the contrary, in Germany the transaction sector fell from 48,5% in 1982 to 41,8% in 1993 [Bischoff i Bohnet, 2000; O'Malley, 2008] introduces a comparative approach for comparing the transaction sector of some countries and points out the difficulties of the cross-national comparisons. According to [Ghertman, 1998] the transaction sector has reached a level of 63% GNP in France, 62% in USA, 56% in Japan and 52% in Germany in 1990.

In the first decade of the new millennium, transaction sector research has also spread over the countries with transition economy. Thus, the transaction sector of research & development has been conducted in Poland and Bulgaria. It has covered the major part of the validity period of their Association Agreements with the EU.

As for Poland, the Association Agreement was signed in 1991 and was valid from 1994 to 2004. In 2004, the country joined the EU based on the 2003 Agreement. The research of Polish transaction sector conducted by [Sulejewicz i Graca, 2005] covered the essential part of the Association period. They show increasing of the transaction sector of Poland from 49.6% in 1996 to 67.2% of GNP in 2002.

As regards Bulgaria, the Association Agreement was signed in 1993 and was valid within the period of 1995-2007. In 2007, the country joined EU based on the 2005 Agreement. The research of Bulgarian transaction sector conducted by [Chobanov i Egbert, 2007] covered most of the Association period.

They use the method of [Sulejewicz & Graca, 2005] to display the growth of Bulgarian transaction sector from 37.4% in 1997 to 52.7% of GNP in 2003 and to make a comparison between the two Associated Countries (Poland and Bulgaria).

The research by [Egbert, Ivanova i Chobanov, 2010] has given more information with regard to the Association period. According to the updated information the transaction sector of Bulgaria provided 36,3% of GNP in 1997, however in 2006 this indicator totalled 51,9%.

Thus, in both Poland and Bulgaria, the transaction sector was essentially transformed over a period of the Association Agreement. In Poland it has increased by 17%, and in Bulgaria it has increased by 15%. The internal structure of the transaction sector has also been strongly modified in these countries.

All these researchers identified the scope of transaction sector with the total value of transaction costs. We will use a different technique to compare the size of the transaction sector in different countries. It presumes identification of the scope of the institutional transaction sector with the volume of transaction activities.

To begin with, it was proposed to compare the volume of transaction activities by employment [Arkhiereiev, 2003]. It turned out, that in Ukraine, 19.3% of those employed are engaged in transaction activities. This index is by far less than the one of developed market economies. It makes up 77.8% of the share of the employed in rendering transaction services in Japan, 75.2% for Italy, 64.6% for Germany, 64.2% for Canada, 61.4% for Great Britain, 53.7% for USA. To compare, the share of the employed in private transaction activities accounts for, respectively, 74.0% for Germany, 61.1% for Italy, 53.4% for Japan and for USA, 50.0% for Great Britain, 48.0% for Canada.

To continue with, it was proposed to compare the volume of transaction activities by a set of different value indexes (Output, Intermediate Consumption, Gross Value Added, Labour Compensation of Employment, Gross Operating Surplus, Net Operating Surplus, Gross Capital Formation, Capital Consumption, Net Capital Formation).

Some years ago, the author has conducted such investigation to compare the transaction sector in Ukraine and Germany by wide-range indexes [Arkhiereiev, 2008] that can also be used nowadays, under the EU-Ukraine Association Agreement.

All other methods provide the comparison of the share of the transaction sector in GNP only. At the same time, the system of national accounts analyzes the institutional sectors of economy with a different set of indicators.

Therefore, the determination of the size and significance of transaction activities, which include only transaction institutional units, can play an important role. The distinctive characteristics of transaction institutional units include their uniformity of behavior and autonomy in decision-making in respect to their transaction functions.

Using different numerous indicators is necessary to allow for a wide-ranging analysis of the transaction activities similar to the analysis of the institutional sectors in the system of national accounts.

The need for new transaction policy in the New Associated Countries like Ukraine is more obvious in comparison with the EU Member States. Carrying out an absolute majority of transactions was monopolized by the government sector of the command economy. The transaction policy was strictly prohibitive unlike in the other countries of the World in relation to private transactions. This policy became the starting point of the market economy formation, which is based on free transacting and private transaction activities. However, public transaction activities do not disappear under market transformation conditions, but they have undergone considerable changes.

The public sector reserves for itself some specific functions such as determining rules and actions of law-enforcement agencies directed to suppression of crimes committed during carrying out transactions as well as the judicial system activities focused on determining the character of punishment of the guilty. Special public organs also play an important role.

In general, the public sector loses its monopoly of carrying out the transactions and is subject to substantial reduction under the market transformation. However, it does not lose its role in general which undergoes a modification in accordance with the general principles of the market economy.

The public sector must provide implementation of its main function to be a reliable instrument of carrying out effective transaction policy, while direct transaction functions pass on to the private sector.

It also concerns international transactions carried out by private sector, but under the influence of Government transaction policy. Signing of EU-Ukraine Association Agreement in Ukraine in 2014 has become important element of Government transaction policy for the years.

Association Agreements with the EU have always exerted a severe impact on the signatory countries, restructuring of their transaction sector being one of

the effects. International political tensions generated by the Agreement with Ukraine are known to be its special feature. Their implications have a much greater influence on the economy than the Agreement itself. The EU-Ukraine Association Agreement is believed to have had a greater geopolitical impact than any other Association Agreement with the EU, its influence being comparable only to the collapse of the Eastern bloc and the disintegration of the Soviet Union in the early 1990s.

The most important distinctive characteristic of the Agreement is rather broad geographic scope of its impact. Naturally enough the Agreement will have the strongest influence upon Ukraine but it will also affect both EU countries and third countries. Restructuring of EU transactions will be definitely influenced by the sanctions imposed against Russia as well as by the so-called Russia's anti-sanctions (the Russian food embargo). They can affect not only a trade turnover with Russia, but also cause other changes with respect to substitution of commodity transactions with Russia. It is natural that among third countries the Agreement should mostly have effect upon Russia. However, the Agreement can indirectly affect other countries. For example, Latin America countries may substitute European products in the market of Russia.

Ukrainian economy as a whole shrunk, as a result of external aggression and an increasing lack of confidence. In the 11-month period (11 months of 2014 compared to 11 months of 2013) is observed an increase in exports by 12%. It is not bad, in comparison with collapse of the exports to the Russian market.

As a result, not only Ukraine but also third countries exert both direct and indirect influence over EU countries including Germany. Seven months statistics have shown that indirect consequences of the Agreement have influenced German-Ukrainian international transactions more than those between Germany and Russia in relative terms.

Another important feature of the Agreement is the power of its influence. In Ukraine influence of the Agreement has appeared to be broader than one would assume even before its signing. The fact is that its signing has caused changes in the political and economic regime in the country. That means that in general the consequences will be more profound than the direct effect. Thus, the effects of the Agreement should be divided into direct and indirect consequences, the latter being caused not by the Agreement itself but by the changes, which took place because of its signing.

These effects are not likely to appear simultaneously. First, since before the Agreement was signed its indirect consequences had already appeared. The Agreement signing itself appeared to take too much time. Accordingly, the con-

sequences are likely to be modified while it is being implemented. Various stages of the Agreement implementation are certain to be observed since free trade regimes are not introduced simultaneously.

Actually even before the Agreement came into operation, certain changes have taken place with regard to external transactions of Ukraine and other countries being involved. Naturally, they will become more profound from now on. The indirect consequences have already become apparent in the first half of the year. Thus, an important milestone in the international trade in Ukraine, was the agreement on the abolition of trade barriers with the EU.

In 2013 as well as during previous period of time major portion of foreign trade was being carried on with CIS countries (if compared to EU) but in the first half of 2014 sharp changes took place and major portion of Ukrainian export fell on EU countries by comparison with CIS countries. In 2013 Ukrainian exports to EU was 10% less than to CIS countries, but in 2014 it exceeded by 2%. This has to do with both the political situation and the removal of trade barriers between EU and Ukraine since May 2014.

Exports to Europe decreased by 36% and to Commonwealth of Independent States by 54 %, first half of 2015 the largest declines are Cyprus (82%), Belgium (56%), Hungary (51%), Great Britain (49%), and Finland (48%). The only two increases recorded Malta (697%) and Slovenia (41%).

However, Ukraine can use this removal of trade barriers, even by providing quotas, not always fruitfully. Thus, quotas provided to Ukraine for 2015 were used on the average by only 20% for half of the year, compared with 60% use of quotas received by Turkey.

Another trend has been observed in the sphere of foreign direct investments. They seriously reduced including those coming from the EU countries.

## **Conclusions**

The Agreement influence will not add up only to regional restructuring of external transactions or foreign direct investments. The Agreement will have non-uniform influence on the development of industries, the possible effects having to be analyzed individually for each industry.

Reorientation of the economy of Ukraine from Russia to the European Union is already fundamentally changing the structure of Ukrainian foreign trade and the international transactions in general.

In addition, it cannot, but have an effect on the sectoral structure of the foreign trade. Traditionally Russia had bought engineering products from Ukraine. Ukrainian industries that could be successful on the European market would be IT products, food, light industries and agricultural products. First of all, enterprises need to get information. It's not simply a question of turning up on the EU border, even if products meet EU standards. They need to do some marketing, some market research. Going back to agricultural products, there is a potential huge EU market for Ukrainian agricultural products – produced in a traditional way, as they used to be in the rest of Europe 30-40 years ago, which can give a very positive nostalgic message to consumers. They need to start contacting with buyers and learn how to sell their products a bit more. So important, that EU markets are different, and the types of goods preferred by Poles or Germans are different from those bought by Spanish or Italians.

The analysis that has been carried out allows concluding that the Agreement is bounded to have the greatest impact on restructuring of the international transactions of a significant number of countries and mostly of Ukraine, where it also caused crucial changes of the domestic transactions. It is possible and necessary to continue investigating the problem of the international and domestic transaction restructuring by different indexes as well, the problem of the competitive international transaction sector and providing appropriate changes formation of its structure under the influence of EU-Ukraine Association Agreement, i.e. the main problem of this article.

The study of transaction sector is still a vital task of economics and requires a more detailed investigation that would allow finding not only the effective boundaries of transaction sector development but also the parameters of transactions structure maximizing economic efficiency under the EU-Ukraine Association Agreement.

The given task of Economics is of particular urgency, taking into account the possible changes as of January 1, 2016. At this point, the economy of Ukraine can experience a double shock. On the one hand, barriers to export from the EU to Ukraine will be removed. That in itself can shock the Ukrainian economy (national manufacturers might not withstand competition from more developed countries in the market). On the other hand, there is a major risk that Russia will nevertheless close the market for the goods from Ukraine that can make this shock double (we might expect the decline in production because of loss of foreign markets). Therefore, we believe such investigation to be extremely urgent and important since it studies the current state of affairs and estimates the Ukrainian economy prospects taking into account the possibility of double shock.



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**PERSPEKTYWY I WYZWANIA RESTRUKTURYZOWANEGO  
SEKTORA TRANSAKCJI W WYNIKU UMOWY STOWARZYSZENIOWEJ  
POMIĘDZY UKRAINĄ A UE**

**Streszczenie:** W artykule przeanalizowano główne wyzwania i wpływ polityki transakcji w sektorze transakcji oraz wprowadzono termin „międzynarodowy sektor transakcji”. Zbadano konsekwencje dla różnych transakcji międzynarodowych i prawie wszystkich procesów transakcyjnych na Ukrainie, spowodowane podpisaniem Umowy Stowarzyszeniowej pomiędzy Ukrainą a UE

**Słowa kluczowe:** krajowy sektor transakcji, międzynarodowy sektor transakcji, Umowa Stowarzyszeniowa pomiędzy Ukrainą a UE.