

2. BILATERAL ECONOMIC COOPERATION OF UKRAINE AND RUSSIA

The key principles of Ukraine-Russia economic relations are specified in the basic Treaty of Friendship, Cooperation and Partnership between Ukraine and Russian Federation (“Big Treaty”) signed by the parties on May 31, 1997, that made the framework for the two countries’ relations. The priority goals of the two states, very much similar, included, in particular: accomplishment of economic reforms and strengthening of national economies; enhancement of the well-being of the peoples of the two countries; integration into the world community as equal and influential partners.

On February 27, 1998, the parties signed the Agreement of economic cooperation for 1998-2007 that approved the Programme of economic cooperation between Ukraine and the Russian Federation for 1998-2007 and a relevant plan of measures. Upon the expiry of the latter, on June 22, 2007, the heads of governments of the two countries signed the Programme of economic cooperation of the Russian Federation and Ukraine for 2008-2010.

Furthermore, the heads of states signed the Russia-Ukraine Action Plan for 2005-2006 and the Russia-Ukraine Action Plan till 2009 that specified priority measures in bilateral relations. Those documents envisage a set of measures aimed at harmonisation of the legal framework of economic relations, deepening Russia-Ukraine cooperation in the trade and economy, fuel, energy and agricultural sectors, machine-building, transport and communications, industrial policy, aircraft building, science and technology, use of space and nuclear energy for peaceful purposes.

The sides have signed and put into effect 58 interstate and intergovernmental treaties and agreements and many bilateral inter-regional and interdepartmental documents in one or another way aimed at development of cooperation in the economic sector.

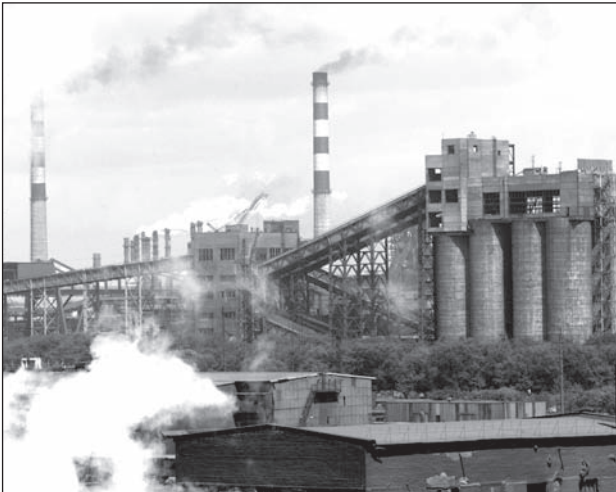
2.1. HISTORY OF ECONOMIC RELATIONS: DECLINE, RISE, STAGNATION

Decline: 1990s. After the USSR breakup, the existing potential of economic ties was derailed, for external and internal reasons. At that, hi-tech branches sustained the greatest losses. For instance, the chemical industry of the former USSR, concentrated mainly in the Russian Federation and Ukraine, ranked among the most powerful in the world. It produced more potash fertilisers, synthetic rubber, ammonia than any other country in the world. Chemical products enjoyed high demand on domestic markets. However, in the post-Soviet period, in Ukraine alone, production of mineral fertilisers fell by 50%, chemical fibres and threads – almost six times, plant protection means – 50 times.

Inability to independently solve economic problems in the conditions of remaining strong mutual dependence of the economies was among the reasons for economic conflicts between Ukraine and the Russian Federation.

For instance, reorientation of the extracting industry to world markets to the detriment of the national manufacturing industry led to reduction of not only domestic production in both countries but also of mutual trade: the volume of bilateral trade from 1996 till 1999 fell from \$14.4 billion to \$8 billion, or by 55.5%, and the Russian share in Ukraine’s exports of goods fell from 38.7% to 20.7%.

While both countries could somehow make up for the reduction of mutual deliveries of end products at the expense of growth of imports of similar products from third countries (although at higher prices than



under normal Ukraine-Russia relations), reduction of mutual deliveries of industrial goods, whose share in the total Ukraine-Russia trade yet in 1993 was close to 80%, could not be offset in principle.

Cut cooperative ties resulted in reduction of hi-tech production, drop in profitability, decline of budget revenues, and consequent deterioration of people's well-being, growth of unemployment and risk of social protests.

To prevent further deterioration of the situation, both states had to make huge efforts for conversion of enterprises to make new products. However, this required significant funds obtained, *inter alia*, from the growth of exports of strategic raw materials to third countries.

Meanwhile, due to employment of different schemes of tax evasion in foreign economic activity by businessmen and lack of effective control of export-import operations, growth of foreign currency proceeds from exports of raw materials could not help fundamentally improve the economic situation, since exports brought profit to business structures rather than the national economy as a whole.

With time, it appeared that the growth of export beyond the CIS cannot make up for losses from the reduction of mutual trade (in particular, because the structure of both Russian and Ukrainian exports to Western markets is dominated by raw materials and products with a low degree of processing, while exporting to each other's markets products with a higher degree of processing).

Rise: 2000-2004 Reorientation of trade relations between the two countries began in 2000, when after a long period of decline growth of mutual trade was recorded for the first time. In 2004, trade in goods between Ukraine and the Russian Federation reached

\$17.6 billion, or 2.2 times more than in 1999. Ukrainian exports to the Russian Federation in that period increased 2.5 times, Russian imports to Ukraine – 2.1 times.

Bilateral trade was promoted by intensification of contacts on the level of heads of actually all ministries and agencies engaged in trade and economic cooperation. Over a relatively short period, the sides managed to solve a number of problem issues in the oil and gas sector, which helped raise deliveries of Russian energy resources to Ukraine: while in 1999, Ukraine imported some 6 million tons of Russian oil, in 2004, its volume exceeded 20 million tons.

In 2001-2002, fundamental bilateral documents were signed, such as the Programme of Transborder and Inter-Regional Cooperation, the intergovernmental Memorandum of principles of non-use of special measures against imports of goods originating from customs territories of the parties, Agreement of strategic cooperation in the gas sector, etc.

With the development of trade relations the structure of Ukrainian export began improving, with a gradual increase in the share of products with higher added value, namely: metal products, whose share in Ukraine's exports rose to 30%, engineering products (26%), foodstuffs (to 17.6%) and chemical products (to 14.1%). By and large, those four branches in 2004 accounted for some 90% of Ukraine's total exports to Russia.

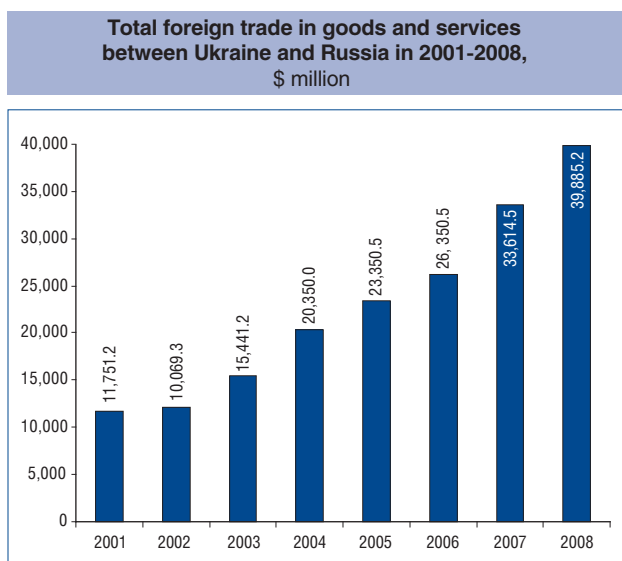
Activity of Russian investors also increased. While on January 1, 1998, their capital in Ukraine amounted to \$152.6 million, by January 1, 2005, it rose to \$457.5 million, or 3-fold. The greatest funds were invested in Ukrainian oil refineries, which improved the situation at those enterprises through their provision with raw materials, growth of production, modernisation of equipment, creation of new working places. Serious investments were made in trade and food industry, processing of agricultural produce. In 2004, Russian capital investments in those sectors of Ukraine's economy increased on the average 1.6 times and made, respectively, \$32.3 million and \$17.8 million.

Russian investors also demonstrated keen interests in the sectors of transport and communications, metallurgy and construction industry, where they invested \$88.9 million, of 19.4% all Russian capital investments in Ukraine's economy. Noting intensification of bilateral economic relations in that period, one should keep in mind that it had a notable political dimension. A favourable for Ukraine attitude of the Russian Federation was largely caused by Ukraine's announced plans of participation in regional integration in the post-Soviet space (EurAsEC, SES) and readiness to meet Russia's economic and political interests.



Steady growth: 2005-2008. Despite cool political relations after the 2004 presidential elections in Ukraine, economic cooperation between Ukraine and Russia continued to grow.

For instance, according to the State Statistic Committee of Ukraine, Ukraine’s total foreign trade in goods and services with the Russian Federation rose, compared to the previous year, in 2006 – by 12.1%, in 2007 – by 28.4%, in 2008 – by 18.7% (Diagram “Total foreign trade in goods and services between Ukraine and Russia in 2001-2008”)



At that, Ukraine’s total foreign trade in goods only with the Russian Federation rose, compared to the previous year, in 2006 – by 10.4%, in 2007 – by 35.1%, in 2008 – by 19.1%.

Noteworthy, in that timeframe, Russia was among a few key partner states with whom the rate of growth of Ukrainian exports exceeded that of imports. For instance, compared to the previous years, in 2006, exports rose by 15.5%, imports – by 7.4%, in 2007 – by 46.4% and 22.1%, in 2008 – by 24.2% and 15.3%.

Although in value terms, imports from the Russian Federation still far exceeded Ukrainian exports, Ukraine’s deficit in trade with the Russian Federation showed a downward trend – from \$5.35 billion in 2006 to \$3.67 billion in 2008.

That timeframe also saw changes in the structure of bilateral trade between the countries. Ukraine’s economy remained dependent on Russian imports, but its structure was dominated by energy resources (in 2007 – 46.8%, in 2008 – 42.8%) and raw materials¹.

Meanwhile, the structure of Ukrainian exports mainly consisted of products of medium and high degree of processing, and services (in 2008, engineering products accounted for 31.7% of all exports to the Russian Federation, metallurgy – 19.6%, services – 19.6%²).

The Russian market remained important and attractive for Ukrainian manufacturers. The Russian Federation accounts for 23.5% of all Ukrainian exports and 22.7% of imports (in 2005, respectively, 21.9% and 35.5%).

Furthermore, the Russian Federation steadily ranked 6th-7th among the main investors in Ukraine. While on January 1, 2006, Russian investments totalled \$835.8 million, at the beginning of 2009 – \$1.85 billion.

Russia invested mainly in Ukraine’s financial sector (growth from \$54.7 million in 2005 to \$672.5 million in 2008), construction (growth from \$19.3 million to \$129 million) and operations with real estate, lease, engineering and services (growth from \$54.7 million to \$151.4 million, Table “Direct investments of the Russian Federation in Ukraine by kind of economic activity”³).

In turn, Ukrainian investments in the Russian economy, at the end of 2005 totalling \$102.9 million, reached their peak of \$148.6 million at the beginning of 2008 and decreased to \$99.9 million by January, 2009.

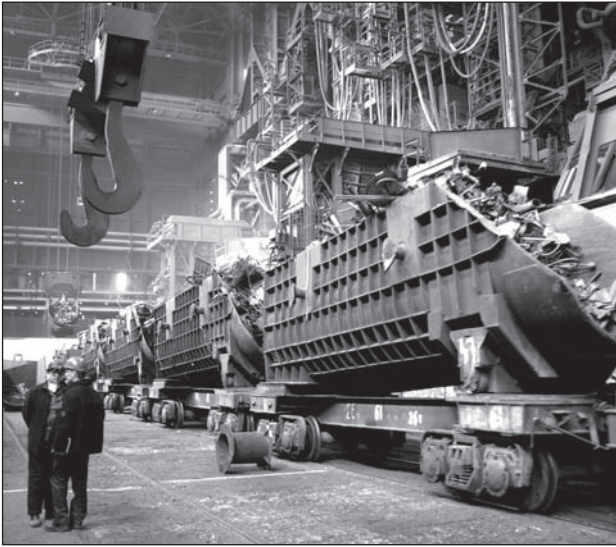
Direct investments of the Russian Federation in Ukraine by kind of economic activity, \$ million

	Investments as of	
	01.01.2008	01.01.2009
Total, in that:	1,462.4	1,851.6
Finance	290.2	672.5
Industry	226.6	245.7
Operations with real estate, lease, engineering and services for businessmen	151.4	162.4
Construction	113.9	129.0
Trade; repair of motor vehicles, household appliances and personal items	106.8	156.8
Healthcare and social assistance	101.0	27.2
Transport and communications	81.0	73.6
Hotels and restaurants	37.4	32.1
Agriculture, hunting, forestry	20.6	18.1

¹ Data of the Ministry of Economy of Ukraine.

² Ibid.

³ Source: State Statistic Committee of Ukraine.



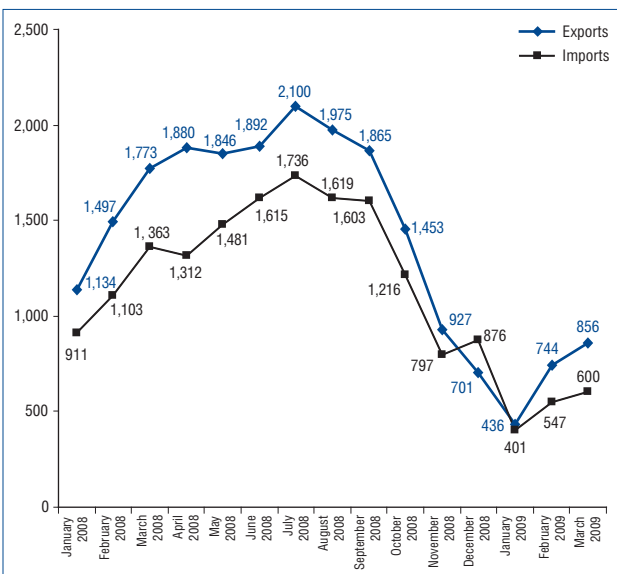
Stagnation: II half of 2008 - early 2009.

The negative influence of the global financial crisis and recession of the world economy could not but affect the trade and economic cooperation between the countries.

Sharp deterioration of the situation on both foreign and domestic markets, decline of production recorded in both countries, devaluation of the national currencies and other factors lead to significant reduction of foreign trade between Ukraine and the Russian Federation, beginning from October 2008 (Diagram “Dynamic of Ukraine’s trade in goods with the Russian Federation in 2008 – I quarter of 2009⁴”).

For instance, monthly exports of Ukrainian products to the Russian Federation fell from \$1.6 billion in September 2008 to \$1.2 billion in October, \$797 million – in November, and \$876 million – in December.

Dynamic of Ukraine’s trade in goods with the Russian Federation in 2008 – I quarter of 2009,
\$ million



According to the State Customs Service of Ukraine, Ukraine’s total trade in goods and services with Russia in the I quarter of 2009 declined, compared to the same period of 2008, by 42.9%, to \$5.28 billion (against \$9.25 billion in January-March 2008).

At that, bilateral trade in goods declined by 47%, to almost \$4.3 billion (in January-March 2008 – almost \$8.1 billion). Exports of Ukrainian products to the Russian Federation declined by 54%, to almost \$1.6 billion, imports – by 58.2%, to nearly \$2.7 billion.

Significant changes took place in the structure of bilateral trade.

For instance, in Ukrainian exports, the share of services increased to 33.6%; decline was observed for engineering products (to 21.2%) and metallurgy (to 13.2%); the shares of foodstuffs (11.4%) and chemical products (7.9%) actually remained unchanged.

Meanwhile, in the structure of imports from the Russian Federation to Ukraine, the share of energy resources reached 66.5%; engineering products declined to 6.2%, metallurgy – to 4.5%.

Noteworthy, present similarity of the branch structures of industrial sectors of both countries makes them compete on both domestic and foreign markets.

2.2. DEVELOPMENT OF INTER-REGIONAL AND TRANSBORDER COOPERATION

Inter-regional cooperation between Ukraine and the Russian Federation is a key to enhancement of the effectiveness of trade and economic relations between the countries, a tool encouraging business entities to search for partners and develop their business on the basis of agreements made between Ukrainian and Russian regions with assistance from the concerned regional administrations.

Nearly 310 documents of cooperation between regions and border areas of Ukraine and the Russian Federation have been signed. However, most of them are of a framework, declarative nature and require actualisation and development of effective mechanisms for their implementation.

Now, the basic documents laying down the principles and approaches of the parties to the development of cooperation in that sector are the Programme of Inter-Regional and Transborder Cooperation between Ukraine and the Russian Federation through 2010, and the Plan of Measures at its implementation.

The most successful measures of the Programme included: implementation of a number of environmental projects; development of the transport infrastructure; creation of business centres; housing construction; development of the tourist and recreational infrastructure.

⁴ Ibid.



An attractive for both parties mechanism of inter-regional and transborder cooperation is presented by the institute of Euroregions. In particular, Belgorod and Kharkiv regions formed “Slobozhanshchyna” Euroregion, Bryansk, Chernihiv and Gomel regions – “The Dnieper”, Kursk and Sumy regions – “Yaroslavna”.

Ukraine-Russian Action Plan through 2009 plans creation of a new Euroregion – “Donbas”, made up of Rostov and Lugansk regions.

Within the Committee for economic cooperation of the Russia-Ukrainian Interstate Commission, the Subcommission for Inter-Regional and Transborder Cooperation was set up, its main tasks being: support for implementation of the above-mentioned Programme of Inter-Regional and Transborder Cooperation; implementation of joint projects on the level of regions; intensification of cooperation within the framework of the existing and creation of new Euroregions; perfection of the regulatory-legal framework of transborder cooperation, etc.

To enhance the economic component of cooperation between border regions, work out a strategy of active development of relations, new mechanisms of cooperative ties among enterprises of the three neighbour countries – Belarus, Russia and Ukraine, in April 2008, the Business Council of Chambers of Commerce and Industry of Byelorussian-Russian-Ukrainian border territories was established.

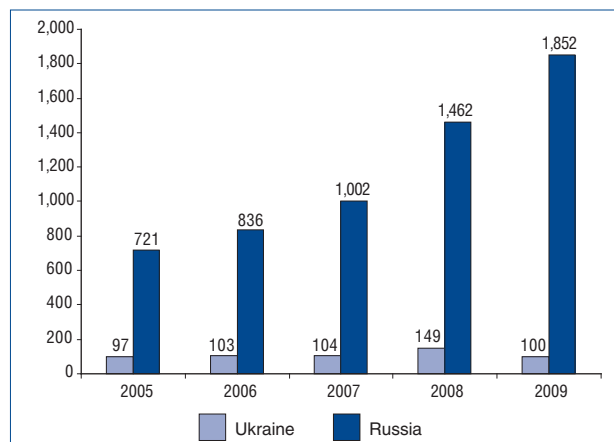
But despite formal progress, inter-regional and transborder cooperation is developing irregularly. Absence of a clear idea of development plans in both states and needs of regions of the neighbouring country, each having its specificity and interests, substantially hampers the potential of involvement in cooperation of not only potentially interested businessmen but also state enterprises.

Another impediment is presented by serious differences in the rights and powers of federal territories of the Russian Federation and regional state administrations of Ukraine, first of all – in budgeting and foreign economic activity.

2.3. COOPERATION IN INVESTMENT SECTOR

Russia remains one of the main investors in Ukraine. As we noted above, the Russian Federation steadily ranks 6th-7th among the countries investing in the Ukrainian economy, Russian investments as of January 1, 2009, totalled \$1.85 billion (Diagram “Dynamic of mutual investments of Ukraine and Russia in 2005-2009⁵”). Russian companies are present in actually all basic branches of the Ukrainian economy (Insert “Russian companies in Ukraine”).

Dynamic of mutual investments of Ukraine and Russia in 2005-2009, \$ million at the beginning of the period



RUSSIAN COMPANIES IN UKRAINE

Especially active in Ukraine are:

- **Alfa Group Consortium** (owns blocks of shares in LynOS (Lysychansk refinery), “Alfa Bank Ukraine”, “Centrenergo”, via an affiliated structure – in “Kyivstar” company, etc.);
- **Lukoil Oil Company** (Odesa refinery, a fuel station network (nearly 200), “Lukor” petrochemical enterprise, etc.);
- **RusAl Company** (Mykolayiv Alumina Plant, Dnieper Metallurgical Plant);
- **Alliance Group** (“Krymnaftoprodukt” and “Khersonnaftoprodukt”, a fuel station network (nearly 180), Stakhanov Carriage Works, etc.);
- **AvtoVAZ-Invest** (Zaporizhya Aluminium Plant);
- **“Sistema” Joint-Stick Financial Corporation** (MTS OJSC (UMC – Ukrainian Mobile Communications);
- **MAIR Group** (Cherkasy, Kherson, Kharkiv, Vinnytsia, Zhytomyr enterprises for collection and processing of ferrous metals);
- **Ministry of Land and Property Relations of Tatarstan and “TatOil” OJSC** (“Ukratnafta” company – owner of Kremenchuk refinery);
- **Smart Holding** (Black Sea Shipbuilding Yard, etc.);
- **Foreign Economic Bank of Russia** (Prominvestbank);
- **“Transmashholding” Company** (“Luhanskteplovov”).

According to the assessments of Russian experts, the Russian Federation owns 223 facilities on the territory of Ukraine, 150 of them – in Crimea.

Strong presence of the Russian capital on Ukraine’s market is conditioned by the following factors: the need of restoration, maintenance and development of production and cooperative ties, prompted by the integrity of the economic system of the former USSR; minimisation of the cost of the core production in the

⁵ Data of the State Statistic Committee of Ukraine.



Russian Federation; access to Ukraine's market; refusal from competition between similar goods on foreign and domestic markets of both countries.

The process was facilitated by the absence of language barriers, similar mentality of representatives of Russian and Ukrainian business circles, similar business practices, and similar conditions of establishment and development of market relations⁶. **Those factors gave and still give representatives of the Russian business circles substantial advantages, compared to investors from other countries (outside the former USSR).**

Gains from the wide presence of the Russian capital include, first of all, restoration of cooperative ties, orders for Ukrainian enterprises, promotion of their products on the markets of Russia and third countries; losses – conservation of obsolete technologies (first of all, in the manufacturing industry), non-fulfilment of assumed investment commitments.

The latter included refusal from construction of an aluminium-producing enterprise in Kharkiv region (a condition of privatisation of Mykolayiv Alumina Plant) and non-fulfilment of terms of the agreement of sale of Zaporizhya Aluminium Plant (the State Property Fund of Ukraine sent a draft official memorandum to that end to the "RusAl" management).

In March 2009, the Lviv Public Prosecutor's Office initiated a criminal case in connection with the intentional non-payment of wages to workers of the Lviv Bus Plants OJSC and evasion of the enterprise officials from payment of insurance premiums for obligatory state pension insurance. In this connection, the Public Prosecutor's Office detained the enterprise owner – Russian businessman I.Churkin.

Privatisation of Ukraine's strategic enterprise "Luhanskteplovoz" by the Russian "Transmashholding" Company was a subject of litigation in connection with violation of the tender rules by the State Property Fund of Ukraine officials.

Officially investigated were also disputable issues dealing with re-privatisation of production assets contributed to Ukraine-Russian joint ventures "Lukor" CJSC ("Oriana") and "Ukrtatnafta" (Kremenchuk refinery).

The presence of Ukrainian capital in Russia is much smaller than of Russian in Ukraine, as it is pressed out by stronger Russian companies.

⁶ Noteworthy, such similarity of the business practices and market relations is not always good and advantageous for national interests of the parties, as it conserves the existing problems: optionality of performance of contracts, unfair competition, tax evasion, grey economy, corruption, etc.

UKRAINIAN COMPANIES IN RUSSIA

The most active in the Russian Federation Ukrainian enterprises:

- "Soyuz-Viktan" Corporation (two distilleries in Moscow region);
- "Nemiroff" Corporation (a distillery in Leningrad region);
- "Industrial Union of Donbas" Corporation (a metal-rolling plant in Armavir and a plant producing MDF board in Krasnodar province);
- "Ukropinvest" Corporation (Lipetsk confectionery);
- "Konti" Company ("Konditer-Kursk" CJSC confectionery);
- "Privat" group (Alpayevsk Metallurgical Plant, Altai By-Product Coke Plant, etc.);
- "Energo" Concern ("Zarechnaya" coal mine in Kemerovo region);
- "Bohdan" Corporation announced plans of construction of a bus plant in the Russian Federation. The project value is estimated at about \$700 million.

The drop of Ukrainian investments from \$148.6 million in early 2008 to \$99.9 million by January 2009, is attributed to the sale of assets and return of borrowed funds by subsidiary companies to their parent structures. According to some analysts, it is more convenient for Ukrainian businessmen to engage in trade operations with Russia than to invest in its economy.

2.4. PROBLEM ISSUES OF BILATERAL RELATIONS IN ECONOMIC SECTOR

More active development of bilateral cooperation is hindered by a number of pending problems in trade and economic relations. In particular, **Ukrainian exporters supplying goods to the Russian Federation often encounter the following obstacles:**

- artificial barriers created for movement of goods, use of tariff and non-tariff restrictions for delivery of products to the Russian market;
- much time and funds needed to get certificates of compliance for Ukrainian goods in Russia;
- unfair competition on the part of Russian manufacturers and importers importing goods from outside the CIS;
- overstated transport fares.

Mutual losses are also caused by **non-coordination of activity on markets of third countries**, especially at export of competing goods (metal products, grain, defence industry products, etc.).

The sides **lack constructivism at solution of disputable issues** arising because of:

- framework nature of many executed economic agreements and absence of effective mechanisms of their implementation;



- preoccupation with own problems, disregarding the interests and restrictions of the counterparty;
- insufficient economic calculation of the effects of some decisions (especially long-term).

The situation is further aggravated by the low awareness of businessmen about the specifics of norms and rules applied by the authorities of both states within their jurisdictions, and shortage of structures that can give them qualified advice and assistance.

Those problems might be gradually solved with the development of cooperative ties, creation of joint ventures and industrial-financial groups. However, the problem lies in the **absence of an adequate regulatory-legal framework regimenting the procedure of cooperation among business entities** and prescribing mechanisms of regulation of bilateral cooperation on the level of business entities and settlements among them.

Furthermore, mutually advantageous cooperation is hindered by lack of funds allocated by states to its promotion, and inadequate information of business entities about the opportunities for cooperation under intergovernmental protocols of production cooperation.

Noteworthy, the share of product deliveries for production cooperation in the recent years has been small – not more than 2% of the total Ukraine-Russian trade.

At the fourth meeting of the Committee for Economic Cooperation of the Russia-Ukraine Interstate Commission (April 29, 2009) the parties agreed to sign the Protocol between the Government of the Russian Federation and the Cabinet of Ministers of Ukraine on deliveries of goods for production cooperation in 2009.

Approaches of the Russian Federation to settlement of trade disputes remain tough and uncompromising.

The main obstacles for growth of Ukrainian exports include tariff and non-tariff restrictions (quotas, sanitary, veterinary standards), antidumping investigations.

This was especially vividly demonstrated by the imposition of a ban on delivery of Ukrainian livestock products to Russia in January 2006. The restrictions hit mainly manufacturers of dairy products (butter, cheese, cream), 90% exported to the Russian market.

Interestingly, by contrast to meat products, where breaches (unauthorised re-export, forgery of certificates, etc.) were recognised by the Ukrainian side, the Russian side lodged no complaints about the Ukrainian dairy products till the imposition of restrictions. Moreover, before the ban, imports of Ukrainian milk and cream were steadily rising.

On August 15, 2008, the Russian Federal Service for Sanitary and Phyto-Sanitary Supervision banned import

of dry milk originating from Ukraine to Russia under the pretext of non-compliance with phytosanitary norms, and again reduced the number of Ukrainian suppliers of cheese.

Noteworthy, a selective inspection of a number of Ukrainian dairy factories conducted in 2008 by the European Union experts also revealed non-compliance of produced cheese with the EU norms, but there were no complaints about dry milk quality.

As of the end of March 2009, 27 Ukrainian enterprises were allowed to export livestock products to Russia, including 14 meat-processing and 13 dairy factories.

Analysis of the practice of application of restrictive measures against Ukrainian products also reveals a **desire of the Russian Federation to limit presence of Ukrainian goods on the Russian market.**

For instance, currently, the Russian Federation has introduced and applies:

antidumping measures against Ukrainian casing pipes (protective duty - 11.4%) and engineering fasteners manufactured by Druzhkivka Metalware Plant;

special measures against large-diameter pipes (special duty – 8%) and fibreglass mesh (special duty – 14.2%).

Antidumping investigation is underway regarding polyamide technical thread originating from Ukraine, **special investigation** – regarding stainless pipes.

Meanwhile, Ukraine introduced and maintains final **antidumping duties on Russian products**: fibreboards (31.58%), asbestos cement corrugated plates (21.8%), abrasive tools (34.6%), ammonium nitrate (from 9.76% to 11.91%), point switches (59.4%).

Specific of restrictive measures used by the Russian side in mutual trade is their clear focus on the most vulnerable sectors of the Ukrainian economy and neglect of agreements of use of protective measures inflicting minimal damage to bilateral trade, as envisaged by Article 3 of the 1993 Free Trade Agreement.

At that, the Russian side is aware that the **Ukrainian economy is more dependent on the Russian market than the Russian economy – on the Ukrainian, and therefore, more vulnerable to the imposed restrictions.** Also in the recent years, **Russia used restrictive measures in mutual trade for political goals.**

For instance, on September 1, 2008, Vice Premiere of the Russian Federation I.Shuvalov instructed concerned Russian ministries and agencies to work out mechanisms for protection of the Russian economy from goods supplied from Ukraine.

Moreover, the Russian media actively discussed allegations about possible cancellation or toughening of the free trade regime with Ukraine by the Russian Federation.



Although officially, it was associated with Ukraine's accession to the WTO, it may be suggested that the true reason for such intentions laid in deterioration of Ukraine's relations with the Russian Federation because of the military conflict in the Caucasus.

Bilateral cooperation on the interdepartmental level faced numerous problems.

For instance, implementation of joint projects in aircraft building was suspended. Despite mutual admission of the utility of joint implementation of An-70, An-140, An-148 airplane projects, the parties failed to come to terms regarding the possible forms of cooperation.

Prioritising modernisation of Il-76 airplane, Russia in fact froze An-70 project and did not fully perform commitments of its funding⁷.

In the hi-tech sector, the Russian Federation toughens access of Ukrainian enterprises to participation in Russian projects (in the space sector) and limits access of Ukrainian designs to the Russian market (modern NPP control systems, An-140 and An-148 aircraft).

On one hand, this reveals the general trend of Russia's scientific-technological policy towards utmost independence in sensitive for the national security sectors, but on the other – those facts may be interpreted as a biased attitude to Ukraine.

Of late, Russia has actively pushed joint projects in the aerospace sector with the USA, France and other EU states. Russia started projects of development of MS-21 medium-range airplane and MTA multipurpose transport airplane.

Noteworthy, the Federal Target Programme "Development of Russian Civil Aviation Equipment in 2002-2010 and through 2015" does not contain a single Ukrainian-Russian project.

While declaring interest in cooperation with Ukraine, the Russian Federation, having established control over Ukraine's "Luhanskteplovoz", pushes talks with Western companies to solve the problem of deficit of the rolling stock at railways.

The Russian side links Ukraine's initiative of a free trade area without exemptions and exceptions with a political decision of Ukraine's subsequent accession to the Customs Union, which is contrary to the course of European integration provided by the Ukrainian legislation.

2.5. PROSPECTS AND LINES OF COOPERATION

In such conditions, the prospects of further development of Ukraine-Russia trade and economic cooperation will greatly depend on the parties' ability to provide for:

- creation of favourable conditions and removal of artificial obstacles hindering the development of mutually advantageous ties;

- promotion of restoration of mutually advantageous cooperative ties on market principles and coordination of actions for protection of national manufacturers and domestic markets from unfair competition on the part of third countries;
- coordination of the parties' actions on markets of third countries to avoid mutual competition, and positions in cooperation with international financial and economic structures and organisations.

For that, the parties should first of all concentrate efforts on the solution of the following tasks:

1. Perfection and simplification of the regulatory-legal framework and mechanisms of economic and foreign trade regulation, first of all, in the fields of taxation of foreign economic operations, pricing, customs, financial, tariff policy, etc.

At that, Ukraine's interests require obligatory consideration of the following principles:

- compliance of mechanisms of regulation of bilateral trade and economic relations with the Russian Federation with the principles working in the European countries;
- simplification of the procedure of certification of goods and quotas on imports in mutual trade;
- approximation of customs and transport fares.

2. Full-scale application of the intergovernmental Agreement of Free Trade between Ukraine and the Russian Federation and multilateral Agreement of the Free Trade Area of the CIS member states. At that, Ukraine's interests envisage:

- observance of the intergovernmental Memorandum of principles on non-use of special measures against imports of goods originating from customs territories of the parties, signed on October 4, 2001;
- development of a mechanism of removal of technical barriers and other restrictions of a similar nature hindering the development of mutual trade;
- continuation of the practice of mutual consultations on market protection means for diminution of possible negative effects for mutual trade;
- resumption of full-scale delivery of Ukrainian meat and dairy products;
- consultations on the state and prospects of bilateral trade in sugar, and on regulation of deliveries of Ukrainian treacle;
- continuation of simplification and unification of national laws.

3. Development of mechanisms of implementation of signed bilateral and multilateral agreements and contracts in the economic sector, first of all, in the field of investment and production-technological cooperation.

⁷ Some aircraft systems and alloys are produced in the Russian Federation, wings – by Tashkent Chkalov Aviation Production Association, entirely controlled by Russia.



As we noted above, the main obstacles for the development of mutually advantageous investment and production-technological cooperation between Ukrainian and Russian business entities ensue from the absence of effective mechanisms and favourable conditions for: implementation of multilateral and bilateral agreements of production cooperation and mutual cooperative deliveries; creation of transnational financial-industrial groups; pursuance of a coordinated structural policy, maintenance of enterprise specialisation; encouragement and mutual protection of investments, etc.

Development of cooperative ties is hindered by trade barriers, absence of effective and transparent mechanisms of cooperation, including sharing of end results of joint activity. **In such conditions, the parties should concentrate on:**

- removal of trade barriers for product deliveries for production cooperation;
- provision of favourable conditions for interaction of enterprises interested in establishment of mutually advantageous cooperative ties, including at construction of facilities in third countries;
- removal of obstacles and simplification of procedures of establishment of Ukraine-Russian joint ventures and transnational financial-industrial groups, first of all, among formerly technologically interdependent enterprises;
- incentives for participants of joint ventures and transnational financial-industrial groups commencing production of new types of products and goods that can reduce dependence of the parties on imports of strategic and hi-tech goods from third countries.

Given the European integration course, it makes sense to employ representatives of the Western states at creation of Ukraine-Russian joint ventures and transnational financial-industrial groups planning production of finished goods in Ukraine for further delivery to the Russian market. At that, the parties' responsibilities might be divided as follows: initial capital and technologies – Western investors, production – technologically related Ukrainian and Russian enterprises, promotion of sales on the Russian market – Russian structure.

4. Implementation of joint activities and projects envisaged by the Programme of economic cooperation of Ukraine and the Russian Federation in 2006-2010

The main problem lies in the lack of funds for implementation of the projects envisaged by the Programme. In such conditions, concentration of the parties on creation of favourable conditions for practical implementation of joint projects, especially of the national importance, acquires particular significance. First of all, this means identification of problems hindering implementation of the Programme and assistance at their solution, including through the use of effective incentives for non-state structures involved in joint projects. Such incentives might include, in particular:

- tax exemptions for enterprises involved in implementation of joint projects envisaged by the Programme;
- preferences for foreign investors already working in Ukraine and the Russian Federation and agreed to reinvest obtained profit in implementation of the Programme projects.

5. Development of scientific-technological cooperation

Ukraine prioritises cooperation in the field of missile and space technology, aircraft building, nuclear energy, radio electronics, ferrous, non-ferrous and special metallurgy, metal processing, advanced materials, agriculture, food industry, resource and energy saving science-intensive technologies, environmental protection.

To enhance the effectiveness of cooperation in science and technology, efforts should be concentrated on creation of common innovative infrastructure, e.g., common innovative-industrial complexes, and perfection of economic and financial mechanisms of innovative activity.

At preparation of an interstate agreement of partnership and cooperation in the field of nuclear energy, it is expedient to work out proposals of participation of Ukrainian scientific research institutions and production associations in development, jointly with Russia, of safe nuclear reactors of the new generation for renovation and further expansion of the base of nuclear energy in Ukraine.

A separate task is to ensure compatibility of software, an automated decision-making system, elements of engineering activity at design of the partner's nuclear units.

Cooperation in the development of technologies of safe disposal of spent nuclear fuel and radioactive waste, design and construction of a storage facility for such materials in the Chernobyl zone should also be a priority for the parties.

Development of scientific-technological ties between Ukraine and Russia also requires proper legal conditions and perfection of the legislative framework in the field of scientific-technological safety, protection of copyrights and intellectual property.

Given the differences in the legislation of the Russian Federation and Ukraine in the issues of ownership of intellectual property rights, to implement joint projects on the basis of licensing agreements between business entities of the parties.

To consider the possibility of creation in Ukraine (Kharkiv) of a Russian-Ukrainian joint venture producing navigational aids and instruments for navigation-information systems.

6. Development of inter-regional and transborder cooperation

To provide for implementation of the Programme of Inter-Regional and Transborder Cooperation between Ukraine and Russia till 2010 and the Plan of measures at its implementation, to envisage a mechanism of their funding and effective control of their performance.