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Ukraine: between the European Union and the Customs Union

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On 10 December, the EU Council stated that an association agreement could be signed with Ukraine in November 2013. However, this depends on the government in Kiev meeting conditions in three areas: making progress on reforms, ceasing its repression of the opposition, and establishing a democratic electoral system.Despite its worsening assessment of the state of democracy in Ukraine, and the lack of success with the reforms, the Union has decided to maintain its cooperation with Kiev, in fear that otherwise the European integration process in the country will collapse.

At the same time the activity of Russia is increasing; their 'Eurasian integration' project is posing a growing challenge to EU policy. On 5 December, President Viktor Yanukovych said during the CIS summit in Ashgabat that "Ukraine should adopt some provisions of the Customs Union of Russia, Belarus and Kazakhstan." In the light of the long stagnation of the Ukrainian economy and the presidential election in 2015, Ukraine should be regarded as more likely to join the Customs Union (CU) now than it was a year ago. If Russia reduces the price of its gas, on condition that Ukraine joined the CU, this would reduce the burden on the budget, and thus finance the social programs that would help Yanukovych to be re-elected.

The EU offers Ukraine one more chance

Currently, the key issue in EU/Ukrainian relations is the signing and implementation of the Association Agreement (AA), which was initialled on 30 March this year; it also includes an agreement on a Deep and Comprehensive Free Trade Area (DCFTA). As a result of the Ukrainian government's violations of democratic standards, the EU refrained from signing the contract, and made doing so conditional on the conduct of the parliamentary elections on 28 October. However, these did not meet the EU's expectations, and Brussels expressed concern about the large number of electoral violations.

Nevertheless, the Council's conclusions of 10 December confirm the EU's commitment to supporting the process of Ukraine's European integration. The document states that the AA & DCFTA could be signed, and the provisional application of certain provisions of these agreements could be started, at the Eastern Partnership Summit in Vilnius scheduled for November 2013. However, this depends on Kiev meeting certain criteria, primarily in three areas: 1) the progress of reforms, with priority given to reform of the judiciary system and economic reforms which would allow the DCFTA to be implemented and improve the business climate, as well as the fight against corruption; 2) providing a democratic electoral system and equal media access for all political forces, as well as the government undertaking dialogue with the opposition; 3) ceasing politically motivated convictions against opposition activists, and respecting the judgements of the European Court of Human Rights on the issue.

Divisions within the European Union on Ukraine

The individual EU member states differ in their approaches to integrating Ukraine. On the one hand, continuing the EU's commitment to Ukraine is favoured by states which are afraid that Ukraine's European integration will fail, as this will mean failure for the EU in the whole Eastern dimension (these are mainly the Visegrad Group countries and the Baltic states, and to some degree the European Commission and the EEAS). They treat Russia's growing pressure on Ukraine to join its Customs Union as an increasingly serious challenge to the EU's interests. Another important element is the economic ties between Ukraine and these countries, and the commercial benefits they bring, which could bring about the possible implementation of the DCFTA.

On the other hand, another group of member states (mainly the Scandinavian and Benelux countries) sees no benefit in deepening EU cooperation with Ukraine, especially as the latter does not respect the principles of democracy. The credibility of the government in Kiev, which despite its earlier assurances has not met the EU's expectations, is low. This raises the concern that deepening cooperation with such a politically and economically unstable country, in which an efficient democratic system does not operate, may undermine the coherence of the Union. Opinions like these are gaining in importance, especially considering the EU's growing internal divisions (into the euro area 'versus' the rest) against the background of the euro area crisis. At the same time, Ukraine's political and economic importance to these countries is limited, and they do not see Russia's rising position in Eastern Europe as a geopolitical challenge.

Is Ukraine moving closer to the Customs Union?

The challenges which the reintegration projects under the auspices of Russia) pose for the EU are even more important in the light of recent statements by top Ukrainian politicians. On 5 December, after a meeting with Russian President Vladimir Putin in Ashgabat, President Viktor Yanukovych said that if Ukraine cannot find instruments for cooperation with the CU, the country will lose a lot, and so implementing some of the CU's provisions would be advisable. But on 10 December, Yanukovych said that Ukraine has begun harmonising its national legislation with the CU's regulations, in order to avoid discrimination against Ukrainian producers and losing the CU market. The Ukrainian media has recently revealed government estimates which show that Ukraine would receive large and almost immediate benefits of membership in the CU. Earlier, the benefits of working with the CU had been mentioned by Prime Minister Mykola Azarov and the deputy head of the Presidential Administration Iryna Akimova, among others. Ukraine's readiness to participate partially in the CU had already been signalled by Kiev, but it did not specify in which areas this would be possible, and how deep such co-operation would be. For its part, Russia is demanding the full integration of Ukraine with the CU, and not just in individual sectors.

So far, the statements by Ukrainian government representatives concerning the CU have been treated as attempts to evade pressure from Moscow, and also as a signal to the EU not to slow the process of concluding the AA. At this time, however, the situation is different. The Ukrainian economy is on the verge of recession, and Kiev's creditworthiness abroad is both limited and conditional on the introduction of unpopular reforms. Meanwhile, the October elections showed a fall in support for the Party of Regions, the group in which Viktor Yanukovych has his political roots. So, the lower Russian gas price for Ukraine (about US$12 billion in 2012) which Moscow is proposing in exchange for Ukraine's membership of the CU is seen as a solution that will enable Kiev to balance its budget. In view of the critical balance of power in the country's presidential elections in 2015, this would allow the Ukrainian government to put off the unpopular reforms, and to finance both the social programs and Yanukovych's re-election campaign.

Ukraine's possible membership of the CU would be problematic for both legal and economic reasons. It would probably require amendments to the Constitution; and economically it would block the possible implementation of the EU's DCFTA, and would require Ukraine's import rates to be raised from WTO levels to those of the CU. This move could well cancel out the benefits derived from membership in the CU. Analyses by non-government economists – in contrast to those from government experts – show that Kiev's gains from CU integration would be much smaller than those derived from introducing the EU's DCFTA as part of the AA.

Ukraine is trying to play on two fronts

The Ukrainian president's statements are part of his current policy of keeping a balance between the EU and Russia, and trying to reap the benefits from both sides. Yanukovych's statements on moving closer to the CU came on the eve of the EU Council's meeting, and can be read as an attempt to put pressure on the European Union, which is working to accelerate the signing of the AA and improve the conditions of the agreement. Viktor Yanukovych is interested in obtaining economic benefits from both the EU (from the implementation of the DCFTA) and the CU (the '3 +1' formula) without making any political commitments. If Ukraine were to associate with Europe, this would require the democratisation of the political system and a limitation of its power, whereas integration with Russia could pose a threat to Yanukovych's political position, as well as the interests of the country's business elite.

However, it is hard to determine where the boundary between the realistic possibility of Ukraine joining the CU, and rhetoric intended to put pressure on Brussels, really is. While a year ago integration with Moscow was unlikely, it now seems more possible, due to the deteriorating economic situation and the upcoming elections. It cannot be ruled out that for these reasons, Kiev is more seriously considering the possibility of joining the CU, and Yanukovych's statements and the publication of the economic estimates are intended as soundings for public opinion. Ukraine is still trying to keep its balance between the EU and the CU, but the economic crisis has rapidly reduced its room for manoeuvre.