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Do Oligarchs in Ukraine Gain or Lose with an EU Association Agreement?

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The future of the Association Agreement between Ukraine and the EU is to some extent dependent on the stance of the Ukrainian oligarchs, the wealthiest circle of businessmen who influence the decisions made by President Yanukovych's government. However, only some of them are likely to extract significant benefits from the agreement, while those linked to Yanukovych might remain indifferent. Poland and other EU Member States should ensure that the effects of the agreement's entry into force are as clear as possible to representatives of big business in Ukraine.

The Political Situation. With three months to go before the Eastern Partnership Summit, the major obstacle facing the signing of the agreement with Ukraine is noncompliance with the three criteria of the EU. The authorities in Kiev are expected to complete judicial reform, to amend electoral laws and to solve the problem of selective justice applied to the leaders of the opposition. The Ukrainian authorities are dragging their feet in meeting these demands. However, not all of the politicians from the government camp are eager to press forward with the agreement, as some oligarchs face risks arising from the implementation of the Deep and Comprehensive Free Trade Agreement (DCFTA), which is part of the deal.

Ukrainian Oligarchs. There are several oligarch groups in Ukraine's current political landscape. The biggest group, the "old oligarchs," have maintained influence on the country's political and economic development for years. The most influential is Rinat Akhmetov, whose wealth, estimated at about $15 billion, stems from the metallurgical and energy industries. He is followed by Viktor Pinchuk ($3.8 billion, pipe mills and ferroalloy plants), and Ihor Kolomoyskiy ($2.4 billion, banking and oil refining). The ruling Party of Regions derives its support not only from Akhmetov but also from media tycoon Dmytro Firtash (whose wealth is estimated at $670 million and is derived from the chemical industry and gas trade).

However, the past three years have seen the emergence of a "new" group of oligarchs nicknamed the "Family" by Ukrainian journalists, because it centres on the oldest son of the president, Oleksandr. It is the "Family" that has gained the most visible control over the financial and law-enforcing blocs of the government in the past two years, as representatives of the "old oligarchs" were gradually ousted from the cabinet. For example, Vitaly Zakharchenko, minister of Internal Affairs since 2011 and Minister of Justice Olena Lukash (as of July 2013) are both close confidants of President Yanukovych. Similar changes happened in Ukraine's diplomatic top flight: Leonid Kozhara, a loyal protégé of the Family, was appointed the new foreign minister after the 2012 parliamentary elections, to replace Kostyantyn Gryshchenko (a career diplomat linked to the Firtash group).

Who Gains? According to the DCFTA provisions, Ukrainian oligarchs are likely to gain short-term economic benefits from the elimination of import tariff duties, which might have otherwise impeded their access to the EU market.

Food producers stand to gain the most. A decrease in duties would be useful to the likes of confectionary giant Roshen, owned by Petro Poroshenko, given that these products are levied import tariffs of about 35–40% in the EU. Lifting import duties would also be beneficial to the Kernel group, owned by Andriy Verevskiy, as his company exports about 17% of its grain and oil to the EU. Likewise, Mironivsky Hliboprodukt, owned by Yuri Kosyuk, could gain from the elimination of both sanitary barriers and import duties, to increase its fowl exports to the EU from the meagre share of 5%. However, these businessmen have little if any influence on the government's compliance with the EU criteria.

Meanwhile, the most influential oligarchs, who dominate the parliamentary faction of the Party of Regions, are not likely to gain much in the short run. The Metinvest Group, co-owned by Akhmetov and Vadim Novinsky, exports steel to the EU, free of import duty. Firtash's Group DF exports about half of its nitrogen fertilisers to the EU, where a duty of 6.5% is levied. The only major Ukrainian oligarch who has limited access to the EU market is Pinchuk, whose Interpipe Holding exports only 1% of its seamless pipes to the EU, due to anti-dumping duties imposed by the European Commission.

A heavy dependency on the export of raw materials is a major reason for the oligarchs' reluctance to support the agreement on purely economic grounds. The DCFTA provisions do not offer tariff incentives to Ukrainian exporters of iron ore (zero import duties) and ferroalloys (low tariffs). Likewise, trading companies controlled by the "Family" currently face few obstacles in exporting heavily-subsidised coal to the EU, as import tariffs are not imposed on this raw material.

Conversely, some of the most influential oligarchs could receive short-term gains from Ukraine's accession to the Customs Union (CU) of Russia, Belarus and Kazakhstan. Protection against an all-out trade war with the CU, threatened by the recent steps of Russian customs authorities, is the main reason why they might consider this option. The tangible risks will, however, stem from a loss of control over tariff policies, which would be handed over to the Eurasian Economic Commission. Likewise, oligarchs such as Firtash who rely on imports of Russian gas, cannot count on the promised low gas prices in the CU, given the likely increase of domestic gas prices in Russia. Last but not least, the future regulatory architecture of the Eurasian Economic Union beyond 2015 is unclear, in sharp contrast with the DCFTA provisions.

Who Loses? The Association Agreement provides for a gradual approximation of Ukrainian legislation to EU regulations, which would require substantial market liberalisation. Such a roadmap might, however, result in resistance from the oligarchs linked to the government, as it threatens to undermine their profit models.

The first point of contention is the overhaul of the public procurement procedures in line with EU requirements. In 2012, the Ukrainian parliament passed amendments to the law on public procurement, which excluded a number of sectors controlled by major oligarchs from open, competitive tenders. The outcome of the amendments soon became apparent: statistics show that 40% of all tenders for procurement of fuels, equipment and services for public enterprises were won by private companies belonging to one of three people—Akhmetov (19%), Oleksandr Yanukovych (17.5%) and Firtash (3.5%). Thus, their vested interest is likely to impede the approximation of public procurement law.

Secondly, the DCFTA provisions on approximation of competition rules require the strengthening of anti-monopoly regulators in Ukraine. However, the Anti-Monopoly Committee of Ukraine tends to be lenient on Ukrainian oligarchs: for example, it failed to block overpriced purchases of natural gas by local authorities from companies owned by Firtash, or to prevent Akhmetov from acquiring big energy-generating enterprises. Likewise, the National Commission of Electricity Regulation was accused of a lack of transparency when it established sky-high prices for electricity generated from Crimean solar power plants owned by the Klyuyev Brothers (businessmen close to the president).

Conclusions and Recommendations. EU Member States, including Poland, have to account for the consequences of the DCFTA's entry into force for Ukrainian businessmen. In fact, the latter will have crucial parliamentary leverage over the reforms necessary for signing the agreement, or could prevent the signed document from being properly implemented. The European Parliament, as well as the Polish Sejm, could reinforce inter-parliamentary links with the Ukrainian Rada, as all major oligarch groups are amply represented there.

Diplomatic channels could also be used. In 2012, Ministers of Foreign Affairs Radosław Sikorski and Carl Bildt met Rinat Akhmetov in Donetsk. EU officials could attempt to persuade other oligarchs of the potential benefits that their businesses (and voters) might extract from the agreement: access to the EU market, assistance from the EU in regulatory matters, and badly-needed investments in infrastructure. It is also conceivable that big Ukrainian business might gain broader access to the North American markets after the EU and the U.S. conclude an FTA.

It is therefore important to prove to Ukrainian businessmen that the structural changes triggered by the Association Agreement will be conducive to their own interests, despite some short-term risks. It should be underlined that the postponement of the signing of the agreement might deprive Ukraine of the expected EU assistance in sectors essential to big business in Ukraine.