

**Macroeconomics**

Roman ZVARYCH

**THE SOCIO-ECONOMIC TRANSFORMATION  
IN UKRAINE AS A PROSPECT  
OF CONVERGENCE WITH  
THE EUROPEAN UNION****Abstract**

For a country which takes transit geopolitical position between the West and the East, the participation in international integration processes is inevitable. In case with Ukraine, such participation will allow a country to ensure economic development and income growth. Membership in the European Union is a main step for transformation and stabilization of the Ukrainian economic development, income growth and life standard increase. Taking into account a substantial difference in the development of EU-15 and EU-10+2 (new EU members), which means income growth and convergence in the long term due to different approaches, for Ukraine it follows that an individual approach to socio-economic development should be taken. Membership in the European Union will be topical in the context of economic development and convergence with the economy of the European Community.

**Key words:**

Convergence, employment growth, gross national savings, international integration processes, labour productivity, net migration, real income growth, risk of poverty, real wages, socio-economic transformation, total consumption spending.

---

© Roman Zvarych, 2008.

Zvarych Roman, Candidate Student, Department of International Economics, Finance and Credit Relations, and Marketing, Ternopil National Economic University, Ukraine.

JEL: E0; F15; F10.

## Introduction

The perspective of EU expansion to East in the conditions of international integration processes and namely the EU accession of new countries became an important catalyst of effective market transformations and positive structural changes in the national economies of these countries. An orientation at the EU's Common Market contributed to modernization of the technological bases of national economies, added dynamism and promoted their competitiveness. The modern international integration processes have been developing in the context of globalization and are its displays. Therefore, the civilizational and objective pre-conditions of modern integration processes are the development of the international division of labour, international economic co-operation and general strengthening of the interdependence and tendencies to organization and efficiency at the level of the world system.

When investigating the dynamics of European integration, the Ukrainian researchers B. Zabarko, A. Kudryachenko, P. Rudyakov and others focus attention on different aspects of the integration process and peculiarities of the new members' accession to the European Community. E. Siskos (2003) marks that in overcoming difficulties the EU member countries achieved corresponding economic and social developments by means of economic instruments and progressive forms of relationships. T. Burlay (2005), in determining the essence and specifics of economic integration processes development in Europe including modern tendencies on the world scale, points to the existence of substantial advantages, which are provided by economic integration for the economic development of separate countries, regions and the entire world. Accordingly, for the countries of transitional type, such as Ukraine, these advantages are more important, as they promote effective socio-economic transformation. Thus, integration into the world economic community gives a chance for less economically developed countries not only to get new possibilities for their economic development (due to forming, reorganization and improvement of the national markets and expansion to other markets), but also to be more effectively transformed and provide economic growth in the long term (due to increased competitiveness). As a result, such growth will perceptibly contribute to convergence of the countries with different levels of economic development by defining the final goal and tasks of economic integration processes in time, as economic convergence between subjects. Consequently, integration in the conditions of interdependence and modern technological development is the precondition for economic convergence of the certain region by means of expansion of the mutually beneficial collaboration between the countries in the process of realizing the respective policy.

New empirical studies prove that the tendency towards income convergence is certainly present in the homogeneous group of countries, and it is fully absent in the case of a differentiated group (D. Ben-David, 2000). O. Gavrylyshyn (2001) and Z. Matkovskyy (2003, 2004) point to many analytical models of real convergence for the CEE countries, as well as there are numerous models of income convergence between the group of CEE countries and the countries of EU-15 (for example, R. Bolduin, 1997; L. Bun and M. Maurel, 1998; F. Bryus, 2001; S. Estrin, 2001; European Commission, 2001; P. Doyl, 2001; A. Lezhur, 2001; K. Martin, 2001; V. Saraevs, 2001; M. Marini, 2003; EEAG, 2004; V. Kaytila, 2004). However, there is not a single study devoted to the aspects of economic convergence between Ukraine, an economically weak country with unstable investment climate, and the enlarged European Union.

In view of this, the article aims to meet the followings tasks:

- 1) to analyse the socio-economic state of Ukraine;
- 2) to select the factor of income growth in Ukraine and its convergence with the European Union;
- 3) to offer propositions on the transformation of income growth policy in Ukraine in the context of the obtained convergence factor.

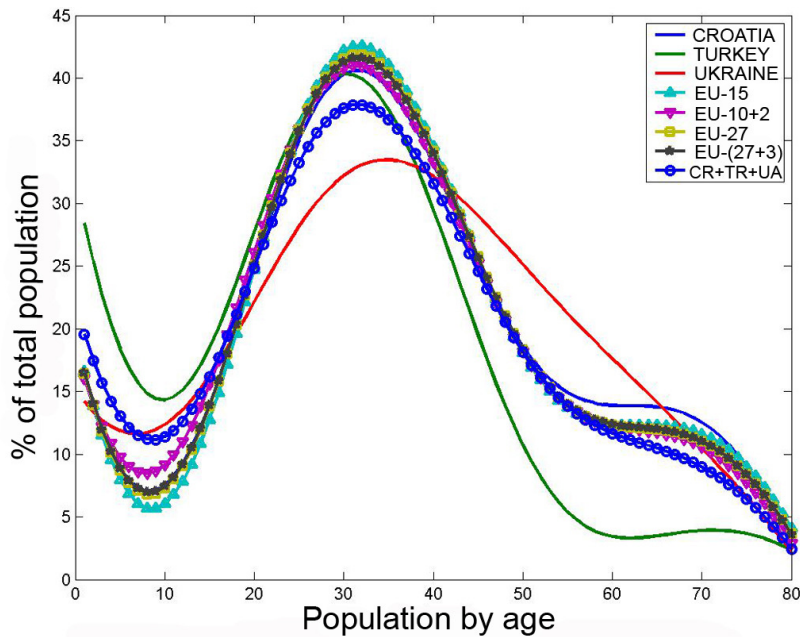
### **The Socio-Economic Situation in Ukraine**

After ten new members joined the EU in 2004 and Bulgaria and Romania in 2007, for Ukraine, which wishes to be a member, the prospects of full-membership in the EU became more real. The socio-economic situation in the country influences on the date and probability of EU accession. The population of Ukraine is 46.6 millions, or 11% of the EU-27 population; population density decreased compared with 1993 and is the lowest in the EU – 77 pers. /km<sup>2</sup>. The forecast population density for Ukraine is negative, in 50 years the slump is expected to make 25%, which means that in the future Ukraine will demonstrate the lowest index in the EU as well. The demographic condition in the EU perceptibly depends on birth rate, which in Ukraine increased between 2000 and 2004, reaching the level of Croatia, whereas in 2005 it surpassed that of the EU-10+2 (12 new EU members) and currently constitutes 985 births per 100 thousand persons. The index is predefined by the mean age of women at childbearing birth, which has swiftly increased in Ukraine since 1996; in 2007 it equals 27 years, which is somewhat less than in the EU-10+2 – 27.3 years and EU-27 – 29.2 years. The high and dynamically increasing index exhibited by Ukraine is typical of the socially developed countries of the European Union. The index is interrelated with the marriages rate in Ukraine – 7.1 marriages/1thou persons, which is the highest in the EU and increasing from 2001, which demonstrates an absolute positive variance; at that, this figure is affected by cultural traditions and the social status of the institute of marriage in Ukraine. Along with positively increasing rate of marriages, there is a more dynamic increase in the rate of divorces in

Ukraine – 3.7 divorces/1 thousand persons, the highest level in Europe. As a result of different approaches to demographic policy in the EU and Ukraine, the population by age class is differentiated enough in Europe, so Ukraine in 2007 as compared to EU-27 looks as a not young country (Figure 1). In Ukraine, the population structure is the following: people under age of 20 – 30.1% (in the EU-27 – 28.2%), between 25 and 50 years of age – 53.5% (in EU-27 – 55.2%), above 65 years – 10.2% (in EU-27 – 13.2%). Certainly, in Ukraine is the most favourable demographic situation due to high percentage of population under 20, which will positively influence the population growth, but EU-27 has a more economically advantageous position because of the higher percent of economically active population. The high social orientation of the European Union’s economy increased the percentage of pensioners, thereby a positive tendency in Ukraine influences on the rejuvenation of EU’s population and on its economic development, especially in the new member countries. Taking into account the high death rate and low birth-rate in the country, the demographic situation can in part be levelled out by the level of net migration, which in Ukraine in 2005 became positive and made +4.0 thousand persons, that was 28% less than in EU-27 and six times less than in EU-15. In this case, the EU should pay additional attention to Ukraine, which is a transition point for the labour force on its way from Asia to Europe.

Figure 1.

**Population by age class in EU, Croatia, Turkey, Ukraine**



Source: Eurostat Year Book 2006-07, Ukrainian State Statistics Committee Yearbook 2007.

The demographic situation in Ukraine substantially depends on its economic development, which partly gives way to the European Union. Thus, level of GDP per capita is by 68% lower than in the EU-27, making 6900 Euros, although the index has been increasing in the long term starting from 2000. As a result, Ukraine should be given essential attention, since its factual development according to this index does not correspond to its real economic potential. The degree of country's trade is the least dynamic in the EU, its export level is the lowest, although it has more than doubled from 1998, reaching 32% of GDP in 2007. The growth of exports occurs mainly due to the availability of a large stock of raw materials, although it can be accelerated by more effective activation of the labour force. The level of imports has grown 2.5 times from 1999, making 38.1% in 2007. In this context, Ukraine should be given due consideration, as the substantial growth of this indicator can take place after the population's income growth in 2008. The inflation level in Ukraine is the highest in the EU: it exceeds the level of EU-27 by 72%, making 12% in 2007, which is the most negative tendency in the last six years. Consequently, Ukraine should be given considerable attention due to substantial, as compared with the EU, depreciation of population's income.

The budget deficit in Ukraine is the highest in the EU, which has been rapidly increasing since 2002, reaching -3.7% of GDP in 2007. Whereas Turkey has decreased its budget deficit by 96.3% in the last 5 years, Ukraine has traded budget surplus for deficit during the same period of time. The tendency for Ukraine is negative, as the country enhances the poverty risk of socially unprotected population. For a long period of time the exchange rate in Ukraine remained steadily in the band between EU-27 and EU-10+2 thanks to proper monetary policy and traditional peg to the American dollar. Thus, the UAH/EUR exchange rate in Ukraine was 6.5005 in 2006, but in result of the mortgage crisis of 2007 in the USA and gradual devaluation of the dollar, it increased in the early 2008 to 7.8004 UAH/EUR. Owing to this the Ukrainian hryvnya is rapidly devaluing against slow increase in Ukrainian exports, which negatively influences the population's incomes and purchasing power. The rate of long-term profit in Ukraine has decreased one and a half times in the long term and reached 9.5% in 2006. Although in the last 15 years the country has realized some positive changes, the high level of the said indicator, which is twice as high as that of the EU-27, points to the unstable investment climate. The Ukraine's sovereign debt is substantially lower than that of the EU-27, although somewhat ceding to the level of EU-10+2. In 2007, the level of sovereign debt in Ukraine was 27.0% of GDP, which means that the country meets the nominal convergence criterion of the EU and can more than double its debt to only approach the level of EU-15 without exceeding the limit of borrowings in the EU.

The employment level in Ukraine is the lowest in the EU, but it has been increasing during the last 10 years reaching 58.1% in 2007 (in EU-27 – 63%). This tendency was caused by positive long-term employment growth, which nevertheless has partly decreased in the second half of 2005. In this context, Ukraine should pay attention to the rate of employment growth that has not in-

creased from 2005, even though the country owns sufficient resource of the labour force, making 1.2% in 2007 (in EU-27 – 2.0%). The unemployment rate in the country has fallen from 10% in 2000 to 8% in 2007. The country demonstrates a quality policy of unemployment reduction; as a result, by the early 2008, the index has been substantially reduced to approach the level of EU-10+2. Along with gradual qualitative changes in the employment and unemployment levels partly increases the country's labour productivity. Although the labour productivity per employee in Ukraine makes 39.1%, which is twice lower than in the EU-10+2 and 2.8 times lower than in the EU-27, it should be mentioned that it has grown since 2001 by 21%. The labour productivity per working hour in Ukraine is by 70% lower than in the EU-12 and twice lower than in the EU-27; moreover, during the last 15 years this indicator has substantially declined. In the country on the whole, this indicator converges with that of the EU-27, but labour productivity still remains four times lower than in Germany and twice as low as in Poland.

In Ukraine, the level of minimal wages, which has been growing since the second half of 2003, is the lowest in the EU making 62 Euros/month in 2007. This indicator in Ukraine is 7 times lower than in the EU-27, and its growth rate substantially lags behind the European one. Along with that, Ukraine demonstrates the greatest growth rate for nominal wages in the EU, which in 2006 was 5 times higher than in the EU-27 and in 2007 partly decreased to 29.2%. The growth of real wages is less perceptible in the country, but is among the highest in the EU, partly lagging behind the nominal wages. In Ukraine in 2005 this index was 8 times higher than in the EU-27, but in 2007 it went down to 18.3% (in EU-27 it fell to 3.3%). This indicator plays a significant role in the income convergence of Ukraine, where the increase in its value is combined with high inflationary processes.

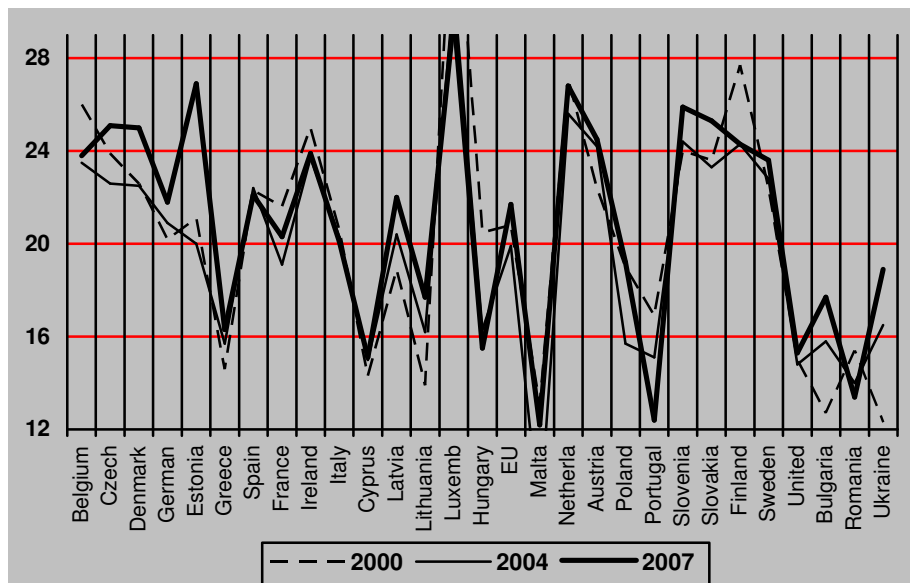
The level of direct taxes in Ukraine has been positively decreasing in the long term, reaching 9.3% of GDP in 2007, which is somewhat lower than in the EU-27 – 11.8%, but higher than in the EU-10+2 – 8.6%. An opposite tendency is peculiar of the indirect taxes, which have been stably growing in the long term, exceeding the level of the EU-27 from 2000 and reaching 15.7% of GDP in 2007. Along with direct taxes, both in the EU and Ukraine increase social contributions. Their level in Ukraine makes 10.1% of GDP, whereas in the EU-27 – 10.9%. The rapid growth of this indicator points to substantial growth of population's income and gradual «de-shadowing» of the domestic economy. There is a gradual increase in Ukraine's governmental compensations, which exceeds the EU-27 level by 4.6% and constitutes 11.3% of GDP (in EU-27 – 10.8%). The level of social transfers in Ukraine has exceeded a similar 1988 index of EU-27, exhibiting long-term growth. The substantial growth of the given index in Ukraine has started after 1986: after the Chernobyl accident almost 5% of the population was granted the status of the persons injured with Chernobyl Accident and the right to social compensation from the state. In 2007 the level of social transfers in Ukraine amounted to 14.5% of GDP (in EU-27 – 10.8%) with a tendency to stabilization. As for subsidies, Ukraine demonstrates an absolutely different ten-

dency compared with the EU. At the time when Europe reduces subsidies to population at high rates by means of replacing them with additional payments and other mechanisms, Ukraine is dynamically increasing their level. Thus, in 2007 such payments in Ukraine amounted to – record in the EU – 5.6% of GDP, in EU-27 – 0.8%. The tendency in Ukraine is negative; in fact, the state enhances the dependence of population on subsidies and provokes high inflation.

Gross national savings in Ukraine are substantially lower than in the EU-27, constituting 18.9% of GDP in 2007 compared with 22% in the EU-27 (Figure 2). Ukraine in this context should be given additional attention, as the negligible growth of index from 2003 points to low income and high consumption levels. Simultaneously with low savings level Ukraine demonstrates high level of total household consumption expenditure. So, the total household consumption expenditure in the EU-27 has been gradually falling since 1996 and today make up 55% of GDP or 10500 Euros per capita, whereas in Ukraine it is 74.5% or 4500 Euros per capita with a partial reduction since 1999. The high value of the index in Ukraine points to the population's low income level and its limited saving capability.

Figure 2.

#### Gross national savings in EU and Ukraine

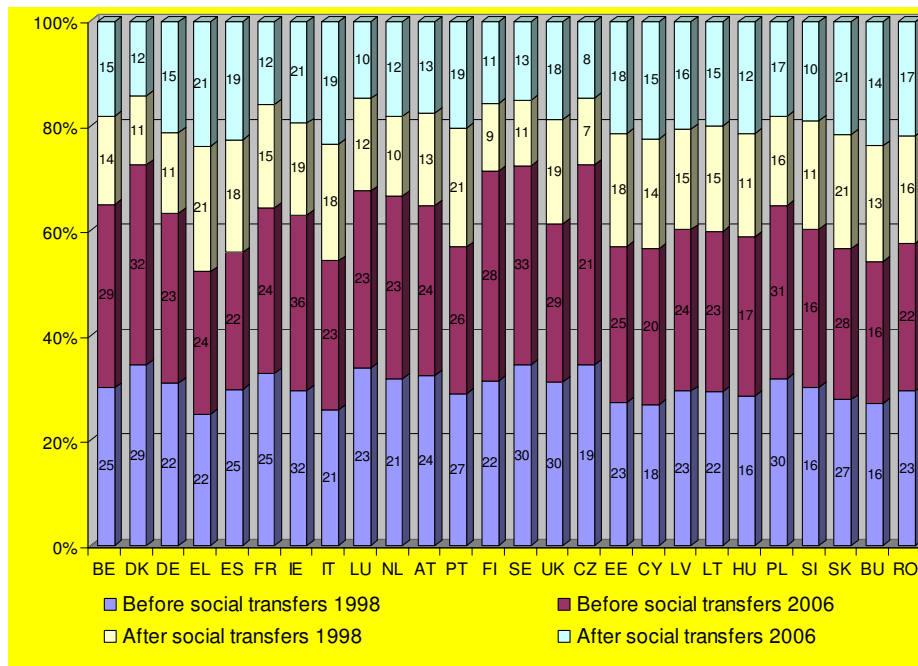


Source: calculate on Statistical Annex of European Economy, European Commission, 2007, Ukraine State Statistical Committee yearbook 2007.

The social protection expenditure has been dynamically increasing in Ukraine from 1999 and achieved in 2007 the level of the EU-10+2 – 16.9% of GDP. This increase has a long-term character with gradual approximation to the EU-27 level which makes 22% of GDP. In Ukraine during the last four years the social protection expenditure has been growing so quickly that it resulted in economic imbalances and inflationary surges, providing the population with only the nominal growth and provoking the risk of poverty. In Ukraine the risk of poverty rate is the greatest in the EU (Figure 3) with 31% before social transfers (male – 29%, female – 33%) and 22% after social transfers (male – 23%, female – 24%); in the EU-27 the respective figures are 23% before social transfers (male – 22%, female – 24%) and 15% after social transfers (male – 14%, female – 17%). In this respect, Ukraine should be given close attention (especially women) because the threat of poverty after social transfers is at the level of EU-27 before social transfers. Such a situation points to high dependence of both Ukrainian and EU-27 citizens on social transfers, as well as to their ineffectiveness, especially in Ukraine, due to high percentage of the population under risk of poverty after social transfers.

Figure 3.

At-risk-of-poverty rate in EU and Ukraine, (%)



Source: calculate on Eurostat yearbook 2006, Ukraine State Statistical Committee yearbook 2007.



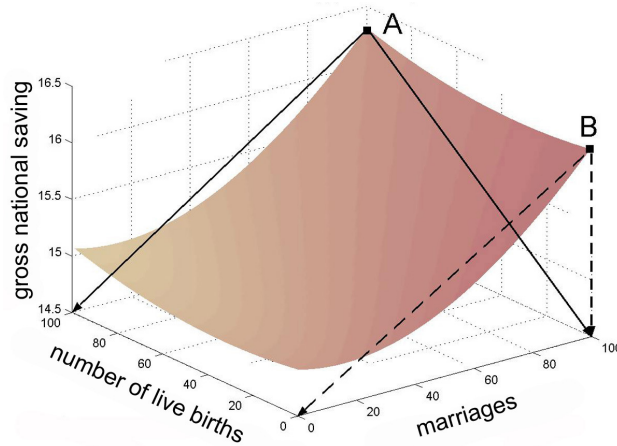
In order to get full membership in the European Union, Ukraine has to confirm its own economic readiness to accession. The degree of readiness will determine the further policy and unfolding of relationships with the Community; in particular, Ukraine should persist in social orientation of the economy, control over the labour market and internal migratory processes resulting from overall growth of population's incomes and their convergence with the European Union. In consideration of the socio-economic position of Ukraine, we can conclude that its current state, especially the level of population's income is somewhat lower than that of the EU-10+2, but their convergence is possible in the long term, especially if to pay due attention to gross national savings. It should also be admitted that Ukraine, the country which geographically borders on the EU, attempts to demonstrate its social orientation of the economy and high income growth following the example of the neighbouring EU member states; however, if such a policy does not find further support in the economic state of the economy, the mentioned income growth will not increase savings, but will be nullified by inflation.

### **The Transformation of Income Growth Policy in Ukraine**

Ukraine has encountered specific demographic problems related to rapid population decline and aging. This process has taken on such a galloping progress that its deceleration will need fundamental changes involving substantial financial expenditures. Today in Ukraine are 21% of people aged 60 or more (and their number will increase) and only 17% of people younger than 14 (their number will decrease). Already in 20 years, the Ukraine's solidary pension system will not bear the demographic load. Savings growth will reduce the risk of poverty, partly stabilize the immigration processes and stimulate the growth of birth rate. The major barrier to household savings growth today is the population's current income level, which is almost equivalent to household consumption expenditure. The growth of marriages in the context of increasing number of live births will have a positive effect on savings (Figure 4). Such qualitative transformations have started to take a place from 2005 and will continue in the future. Ukraine is ranking in the top positions by the number of marriages in Europe since 2001, leaving Croatia and EU-10+2 behind in 2005 by the ratio of live births to total population. Such changes in the demographic policy of the state are fundamental, because even one child birth in a family nearly doubles the risk of poverty. In our society, families with children make up the majority of poor families. It is important that in Ukraine, there is a direct dependence between savings growth and number of marriages in the context of insignificant dependence between savings and births. This testifies to significant changes in the nation's mentality towards savings after marriage registration, especially taking into account minor effect of divorces on the level of savings. The state priority should be to ensure that every citizen makes this transition imperceptibly, keeping the qualitatively stable consumption level.

Figure 4.

Gross national saving in Ukraine



Ukraine, having the geopolitical position it does, is «doomed» to be a transit territory on the way of migrants from the countries of South and South-East Asia to the West. Taking into account that some part of them will unavoidably remain in our country and the number of births grows, the savings level will increase also (Figure 5). In Ukraine, there will be a direct dependence between the level of migration and birth rate and the level of savings. On the one hand, the growth of social payments to parents after birth of a child will suffice to cover the expenditures on its support during a three-year period, allowing parents to save; on the other hand, an increase in net migration will reflect not only the arrival of labour force from the East, but the return of the Ukrainian workers from abroad as well. In both cases, the state will benefit as the nation will partially and rapidly rejuvenate, and the guarantee of social payments will increase, including payments for child support, thanks to taxes and social contributions paid by emigrant workers. On the other hand, the growth of savings might be threatened if the number of live births increases in the context of minimal growth of net migration and vice versa. The dependence between the indicators of net migration and marriages and the growth of savings is somewhat different (Figure 6). In conformity with this dependence, the maximally possible effect of savings growth can most probably result from fast growth of marriages and minimal growth of net migration. The minimal level of net migration means that the population grows due to return of the Ukrainian workers. According to still not the most pessimistic forecasts, by 2050 the population of Ukraine will shrink by another 10 millions.

Figure 5.

Gross national saving in Ukraine

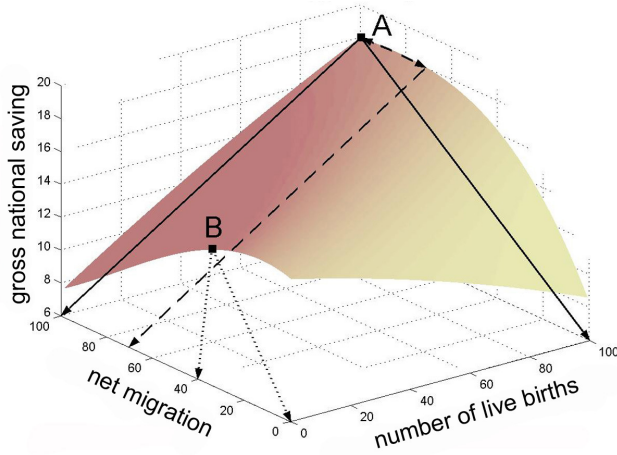
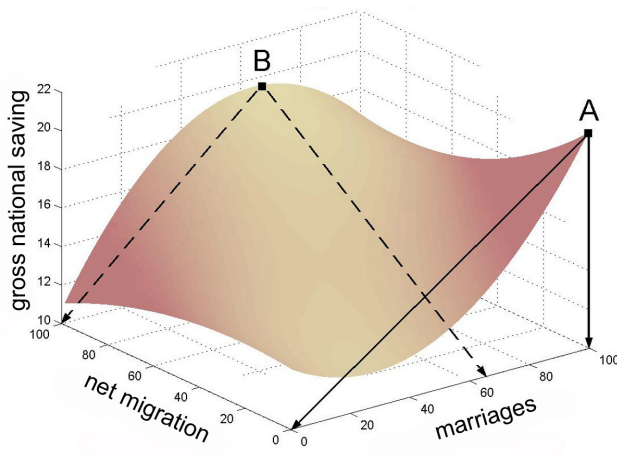


Figure 6.

Gross national saving in Ukraine



Naturally, the largest state in a centre of Europe will not remain unpopulated, – we should therefore expect the rise in migration from the countries that find Ukraine economically attractive. In this context, the highest possible migration level will have a most positive effect on savings if the level of marriages remains at the 7.5 registrations per 1000 persons (60–70%), which is most probable, especially in the conditions of decreasing all-European index. From the standpoint of labour influx, this is not bad. For family considerations, however, it should be taken into account that immigrants from the countries with high birth-rates stick to their traditions in the new country as well. If the number of such immigrants exceeds the threshold of 7-8% of total Ukrainian population, it will stimulate higher fertility in the country and thus lead to increased savings.

At that, keeping marriages at the level of 7.0–7.5% (50–70%) will also be important in the conditions of all-European growth of the mean age of women at childbearing (Figure 7). The mean age of women at childbearing has been swiftly growing in Ukraine during the last fourteen years, as a result, this index grew from twenty five to twenty seven years and this tendency will take a place in the future. A substantial influence on the index has the European tendency towards gender equality, career support and gradual change of women's status in family and society. The Ukrainian society – unlike the economy – is much faster integrating into the European habits, fashion and culture, thus influencing the growth of the index. A positive factor for Ukraine will be a minor fall in savings in the context of increasing mean age of women at childbearing in the long term; therefore, these demographic processes will not produce perceptible damage to the economy. More importantly, another side to the problem will be to provide positive population growth in result of an increase in the number of live births. The social sphere has the most significant influence on the control over demographic problems, the solution of which will be a tortuous challenge for the government.

The growth of savings will characterize positive changes in the economic sphere of the country, substantially accelerate the participation of Ukraine in the international integration processes and stimulate the population's real income growth. In Ukraine, there is a strong interdependence between savings and current taxes, especially in the conditions of increasing current market prices (Figure 8). The volume of indirect taxes in comparison with GDP gradually increases, by much exceeding the level of the European Union, but partly yielding to Croatia and Turkey. The gradual stabilization of the index is expected in the long term, which will result in full WTO membership and signing of a free trade area agreement with the EU. The level of direct taxes in relation to GDP in Ukraine has substantially decreased, partly surpassing that of the EU-10+2, which indicates a stable descending tendency for the next ten years. The main reasons for the recession are the dynamic GDP growth during the last three years, liberalization of tax policy for investor attraction, creation of free economic zones, and adjustment of the Ukrainian legislation for WTO membership.

Figure 7.

Gross national saving in Ukraine

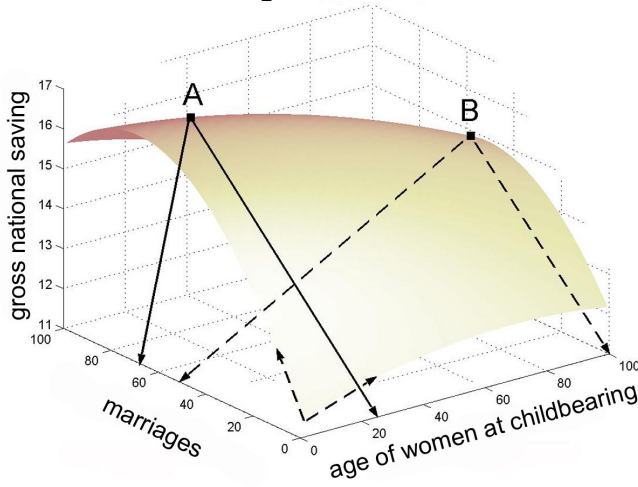
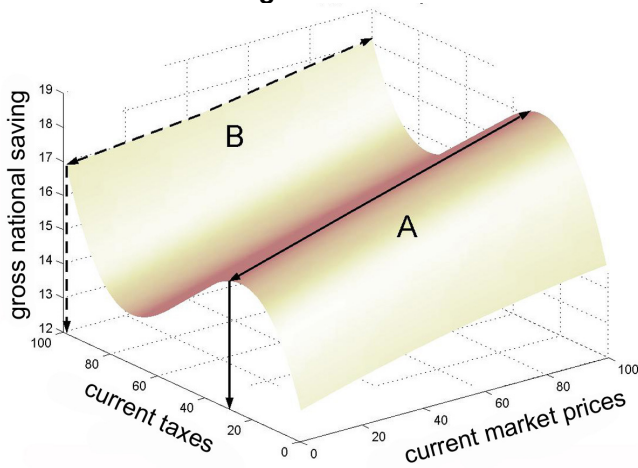


Figure 8.

Gross national saving in Ukraine



In this context, the optimal level of taxes for next five years would be the current 9.7% (30%) of GDP, which will provide for maximal growth of savings, especially in the conditions of surging current market prices. On the other hand, the uncontrolled level of current market prices can be negatively reflected on the income growth level in relation to real compensation per employee index (Figure 9). The impact of maximally possible market prices growth can be relatively positive under condition that the government takes adequate response measures, such a situation will require the maximization of real compensation per employee level. On the other hand, such maximization will substantially burden the budget of the country and will not contribute to its economic development, which in its turn will involve short-term changes in the social sphere of the country. In order to get a long-term positive effect, the growth of current market prices over the next few years should be kept at the optimal 15% (70%) or less, and simultaneously, the support of real compensation per employee growth should be no less than 9.1% (30%). The Ukrainians' income level has been most negatively affected by sudden shifts in the current market prices during the last five years. The basic threat consists in their unexpectedness; therefore, in this relation the government should target its activity at forecasting of the objective necessity for price increase and their gradual and smooth adaptation for the population. The process of economic transformations in Ukraine and the need for support of economic growth requires that the chosen development strategy be reconsidered in the context of fundamental correction of the incomes – the focus on support of socially sensitive layers of population should be redirected towards stimulation of effective economic activity of the able-bodied citizens. The state policy directed at poverty reduction and aggregate national savings growth should provide for the transition from use of cheap labour towards creation of an institutional environment for growth of population's incomes and economic activity, and reduction of the income gap. In the context of income and savings growth, and also partial convergence with the European Union, an important question for the next ten years will be the creation of new workplaces and growth of employment, which is one of the lowest in Europe (Figure 10). Taking into account the optimally possible during the next five years growth of real compensation per employee at 9.1% (30%), it is necessary to provide for maximally possible employment growth in order to maximize savings. The providing of a relatively low growth rate of real compensation per employee will also be a difficult task for the government. It requires that the complex of measures aimed at reforming the labour remuneration system is realized. In the direction of social insurance improvement and pension reform, it is necessary to ensure the gradual convergence of minimal state guarantees to the living wage. It will be important to improve the legislation on the procedure and criteria for determination of the minimal wage and to legislatively provide for the introduction of minimal hourly wage as a state social standard. In order to raise the remuneration of labour for the public sector employees, as well as to remove wage disproportions between positions and branches, it is necessary to introduce the second implementation stage of the Single Tariff Scale.

Figure 9.

Gross national saving in Ukraine

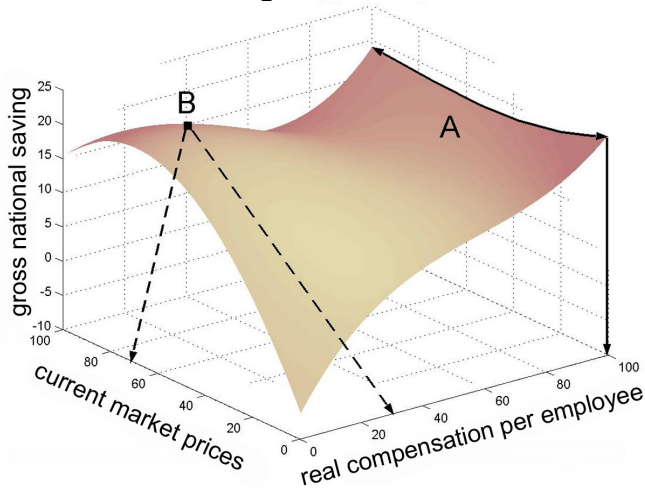
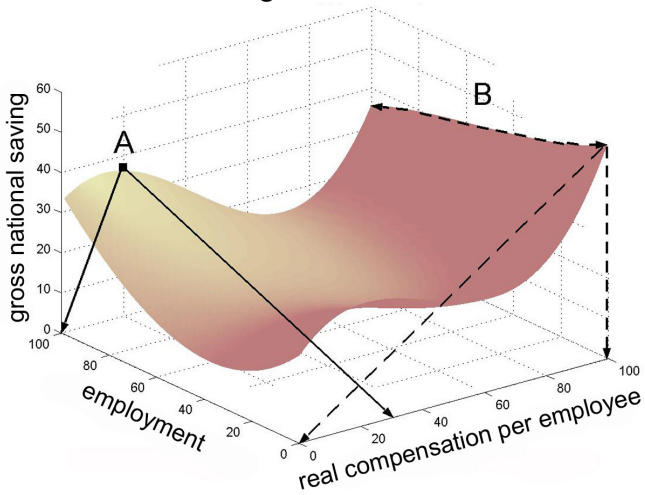


Figure 10.

Gross national saving in Ukraine



To decrease the loading on the payroll fund, tax payments and contributions should be redistributed between employers and employees and the tax base expanded; in addition, the structure of insurance contributions to social protection funds should be redistributed between employers and employees, with simultaneous rise of wages. It is necessary to ensure the protection of the workers' right to receiving their wages in time and in full, as well as to provide for the cancellation of accumulated wage indebtedness. It is also necessary to fully implement the system of personalized accounting and create the automated system of insured persons' accrued pension accounts and pension assets monitoring. Finally, the state should also have a flexible tax policy aimed at encouraging employers and employed citizens to voluntary additional savings in the non-state system of pension providing, as well as inform the population about non-state pension providing and developments in the system of non-state pension funds.

Ukraine is characterized by the low level of employment in Europe, substantially yielding to the European Union and only partly passing ahead of Croatia and Turkey. The positive advantage is the partial growth of the index, although Ukraine has been demonstrating a negative descending tendency in employment growth since 2005. Growth of exports can become a substantial stimulus for providing high employment. Moreover, export growth will stimulate savings (Figure 11). Taking into account that labour productivity in Ukraine is the lowest in CEE and almost three times lower than in the EU-27, it is possible to talk about significant growth of employment in the context of export growth. In the direction of solving the problem with employment, the state should expand the scope of labour use by creating new workplaces, assure the realization of the National Small Cities Development Programme in order to solve employment problems on depressed territories, in particular in small multifunctional cities and coal-mining regions; stimulate the creation of additional workplaces for peasants by developing alternative activities, for example «green» tourism, reviving folk trades and handicrafts in rural localities with the help of preferential financial-credit mechanisms; apply the systems of government orders and paid social works in order to increase employment; improve social support for unemployed persons registered at state employment service in order to ensure their return to productive labour. As for the problems of national exports, it is important to focus on its structure, which needs to be changed from raw-materials-oriented exports towards exports of final products. The priority for the next ten years will be the development of Ukraine's export orientation at the sale of bio-diesel oil and electricity. The availability of large labour and land resources will provide for the arrival of large TNCs, especially in the context of international fragmentation of production and WTO accession.

The realization of drastic alterations in the economic and social spheres will require sufficient financial resources. If during the next five years such resources can be provided owing to privatization processes, in the long (more than ten years) term, the basic function of stabilization and economic development will be played by the national debt. During the last eight years, Ukraine has substantially reduced its national debt, and this tendency will be present during the next five years. By taking a course at long-term economic growth, the country will be able to count on increased



volumes of the national debt, especially in the conditions of sizeable budget deficit, without damaging the growth of national savings (Figure 12).

Figure 11.

**Gross national saving in Ukraine**

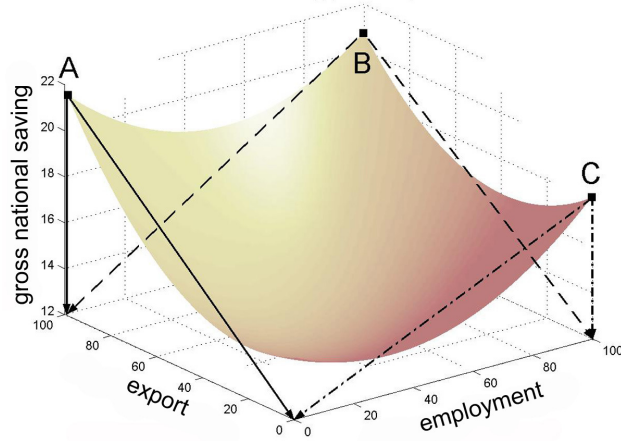
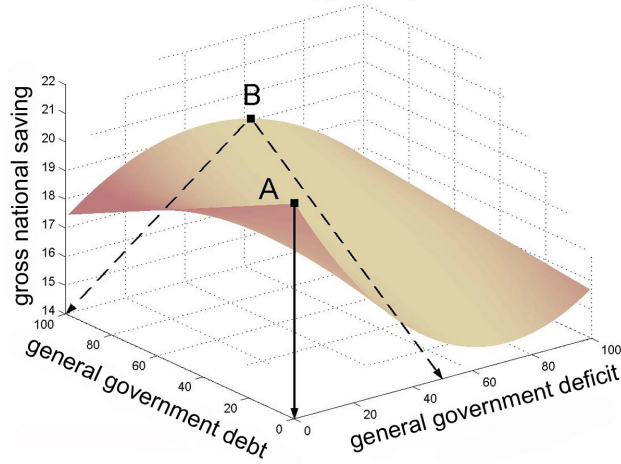


Figure 12.

**Gross national saving in Ukraine**



The next five-year period, which should provide economic stimulus primarily due to privatization of large strategic objects, such as Ukrtelekom, Odessa Port Plant, Ukrzaliznyca and others, will be ideal for growth of savings. In the long-term perspective, no substantial threats are supposed to appear for Ukraine, especially if to take into account the low percentage of national debt and considerable disuse of IMF borrowings quota. The essential growth of budget deficit should be restrained by the activation of national borrowings at the level not higher than  $-4.5\%$  (50%), which will be a critical starting point for gradual fall of savings.

The inflationary processes which take a place in Ukraine are the highest in Europe and will remain stably high in the long term. On the other hand, Ukraine's WTO accession should bring positive economic changes, but will negatively affect the competitiveness of domestic producers in certain industries (agricultural, industrial, textile, food) on the internal market. Such a situation negatively influences the income level and especially the growth of savings (Figure 13). Taking into account the government's gradual withdrawal from the policy of protectionism and gradual shift to market relations, the urgent question of the next five years will be the control over the inflation rate. The optimal inflation rate during the next five years will be no more than 12% (10%), at which the state will provide the constantly high level of savings and will not depend on gradual growth of imports. The basic factors that will stimulate inflation will be the world price increases related to exhaustion of resources and the growth of labour remuneration. An important role will belong to the state monetary policy targeted at controlling the hryvnya/dollar peg in context of the dollar's global devaluation. The proper policy of social transfers, subsidizing and social protection, as well as integration of Ukraine in the world economic market will be of vital importance. In the conditions of deeper integration of Ukraine into the world market and WTO accession, the level of imports will grow in the long term. If keeping inflation at an adequate rate makes savings not largely dependent on imports, the growth of gas prices will make such dependence more tight (Figure 14). During the last eighteen years, the main part of the Ukrainian imports accounted for natural gas. The production of GDP in Ukraine is the most energy-intensive in Europe, which negatively influences both the country's exports and competitiveness. Taking into account the substantial dependence of the domestic producer on this resource and the consumption of gas at the lowest prices in Europe, one can expect the substantial growth of prices in the short-term period. For savings growth, taking into account a considerable increase in gas prices, it will be optimal to accumulate imports. In this situation, an important task for the government will be the reduction of the share of natural gas in the total volume of imports due to gradual realization of energy-saving technologies and development of own natural gas deposits on the territory of the state. In addition to gas issues, Ukraine exhibits systematic and essential price jumps for fuel. The automotive fuel price surges noticeably affect the income level and especially gross national savings (Figure 15).

Figure 13.

Gross national saving in Ukraine

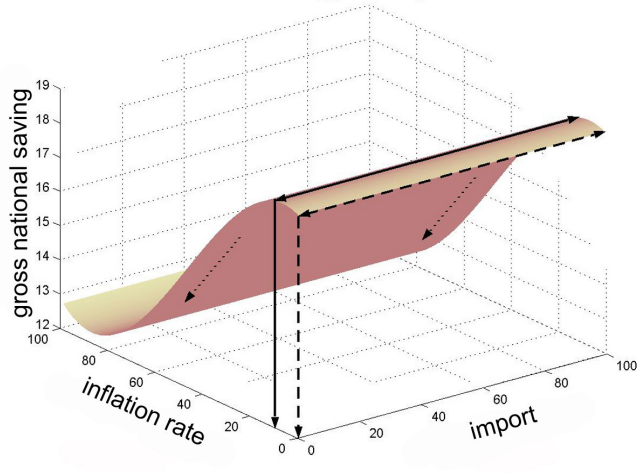


Figure 14.

Gross national saving in Ukraine

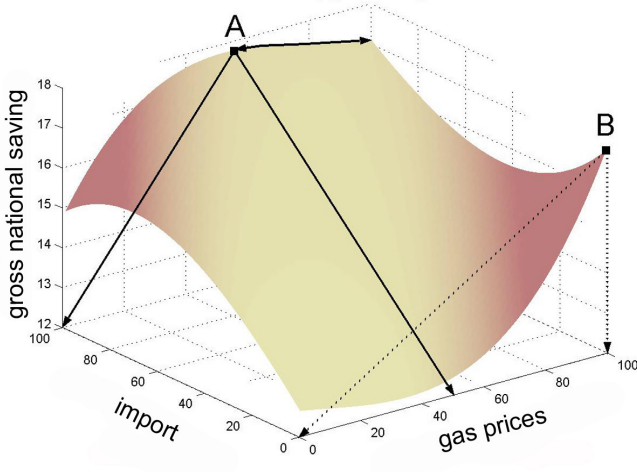
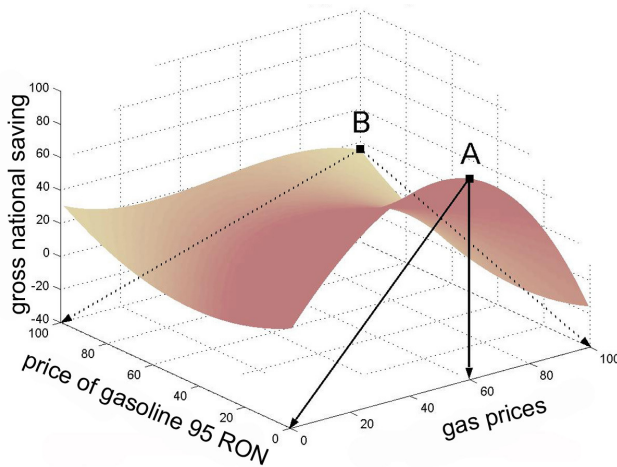


Figure 15.

**Gross national saving in Ukraine**



The growth of fuel prices will have a long-term global nature due to gradual exhaustion of the resource. In this case, Ukraine can expect gradual growth of prices for domestically manufactured products, which can be restrained by application of the newest technologies, rise in labour productivity, and use of alternative energy sources. The abundance of land resources in Ukraine can give the country an opportunity to become one of the major exporters of bio-fuel in Europe in the near future, which will fill the budget and diversify the country's energy dependence. The diversification of energy supplies and their partial production should ensure the country's long-term economic growth and development, as well as income growth and convergence with the European Union.

**Conclusions**

The participation of Ukraine in the international integration processes, especially with the European Union, will allow the country stably develop thanks to the set long-term goal and the proper governmental policy in social, demographic and economic spheres. Taking into account the considerable difference in the income levels between EU-27 and Ukraine, the most essential question for the next ten years, except for the population's income growth, will be its dynamic convergence with the European Union, which should be provided within the next five years by the savings growth. Partial economic changes have taken place in Ukraine since 2005, but the most essential changes must take place

during the next five years. Ukraine's economic development in the period until 2012 must give the answer whether the country can claim membership in the European Union or it is to diverge even more from the Community. If this period does not bring essential changes, it will become possible to speak of the lost chances of full integration in the European society, which means that Ukraine will follow the model of catching-up economic development typical of the countries of Latin America. The advantage of full integration in the EU foresees not only Ukraine's economic growth, but also formation of it as a full economic player on the world market, as well as its social development and income growth. The primary step on the way to solving this problem should be the legislative definition of the poverty index, which must be based on the socio-economic assessment of specialists and experts. Having defined the number of people living at or near the poverty line, the government will be able to properly distribute payments for social protection, and thus make a significant step towards forming the middle class. Formation of the middle class, in its turn, means growth of savings, development of the banking sector, growth of imports, capital inflows, decreased risk of poverty, adaptation of economy to prices growth, and stable high and timely incomes. The establishment of a free trade area between the EU and Ukraine is an adequate reaction to those high-quality changes that have been taking place in the country since 2005. The economically correct incentive for Ukraine's integration in the European Union will be the dynamic income growth and convergence, everything else is only technical matters.

### Bibliography

1. Держкомстат України, 1998–2007. – <http://www.stat.gov.ua>
2. Зварич Р. Є. Конвергенція ринку праці нових членів ЄС // Збірник тез доповідей II Міжнародної науково-практичної конференції студентів та молодих вчених «Інтеграція України у світовий економічний простір». – Тернопіль: Економічна думка, 2008. – С. 199–202.
3. Зварич Р. Є. Соціальний розвиток Європейського союзу // Збірник тез доповідей IV Міжнародної науково-практичної конференції молодих вчених «Економічний і соціальний розвиток України у XXI столітті: національна ідентичність та проблеми глобалізації». – Тернопіль: Економічна думка, 2008. – С. 45–47.
4. Зварич Р. Є. Україна: перспективи номінальної конвергенції з ЄС // Збірник тез доповідей II Всеукраїнської науково-практичної конференції студентів, аспірантів та молодих вчених «Особливості інтеграції України в світовий економічний та політико-правовий простір». – Маріуполь, 2006. – С. 213–215.
5. Матвійчук Я. М., Буяк Л. М., Паучок В. К. Регуляризована ідентифікація функцій економічної поведінки за експериментальними даними // Нау-

- ковий вісник Чернівецького торговельно-економічного інституту КНТЕУ.  
– Чернівці: Книги-XXI, 2007. – Вип. IV. Економічні науки. – С. 412–415.
6. Фойгт Наталія. Формування демографічного потенціалу як передумова реалізації європейського вибору України // Економічний Часопис-XXI, № 1–2. – 2005.
  7. Роберт Казімір. (2003). Історія Європейської інтеграції. Від декларації Шумана до розширення на Схід – Перемишль, Польща.
  8. Ben-David D. Trade, Growth and Disparity Among Nations, in: Trade and Poverty, Geneva: WTO, 2000.
  9. Brucker, H. (2000): Konvergenz oder Divergenz? Wachstumstheoretische Überlegungen zur wirtschaftlichen Entwicklung in den Transformationsländern Mittel – und Osteuropas. Schriftenreihe des Vereins für Sozialpolitik, forthcoming.
  10. De la Fuente, Angel. 2001. Convergence across countries and regions: Theory and empirics. EIB Papers 5, 2, S. 25–45.
  11. Europe in figures – Eurostat yearbook 2006-07. – <http://ec.europa.eu/eurostat>
  12. Matkowski Z. Economic Situation of Post-Socialist Countries: Economic and Social Effects of Transformation (in Polish), Ekonomista 6, 2003, p. 737–774.
  13. Matkowski Z., Prochniak M. Real economic Convergence in the EU accession countries, in: New Europe: Report on Transformation, Warsaw, 2005, p. 121–131.
  14. Mountford, A. (1998): Trade, Convergence and Overtaking. In: Journal of International Economics, Vol. 46, pp. 167–182.
  15. Romer P.M. Increasing Returns and Long-Run Growth // Journal of Political Economy 94, 1986, p. 1002–1037.
  16. Statistical Annex of European Economy, European Commission, 2007. – <http://www.ec.europa.eu>.