

THE UKRAINE AND CHINA INTERNATIONAL TRADE COOPERATION: IMPACT ON THE UKRAINE TRADE DEFICIT

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Abstract

The research is dedicated to uncover the reasons of Ukrainian international trade inefficiency, measuring of the China's role in current account imbalance. The analysis of current account and net exports are compared with the GDP growth and the structure of savings and investments in Ukraine.

Key words: *current account, net exports, competition strategy, competitiveness, strategy of import substitution, inequality in foreign trade.*

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1. INTRODUCTION

Ukraine is situated on the edge of crucial transformations of economy – the market economy in a headline, but uncertainty in international trade. The trade balance is negative, and the economy has dependence to imports. The market or government failed to establish the effective management mechanism of industrial and resource-abundant country, which still doesn't have productive competition strategy of economic development. The cooperation with global markets is based on the global market conjuncture, which transfers the global market risks into the economy of Ukraine without significant outcomes in economic development. In fact, there is no economic development in the Ukraine, which is not concerned with international business (mainly transnational corporations). The high rate of energy dependence of imports is main factor of low competitiveness for Ukrainian industry and social sphere. The cooperation with developing countries like China is the most promising international course of economic development but it is also a great challenge for countries with low competitiveness, like Ukraine.

The theoretical basis of international trade and competitiveness theory was created by A. Smith, D. Ricardo, E. Heckscher, B. Ohlin, P. Samuelson, W. Leontief, M. Porter and others. The practical aspects of China with different countries competitiveness and international trade balances were developed by following authors: Justin Yifu Lin, Hinh T. Dinh, Fernando Im, A. Subramanian, Banu Setlur, Ayala Peled Ben Ari, M. Amity, L. Castro, M. Olarreaga, D. Saslavsky, M. Pigato, D. Lederman, E. Rubiano and others.

The deficit of net exports and current account is typical for Ukrainian economy for a significant period. Nevertheless, inequity in social and economic structure in Ukraine has

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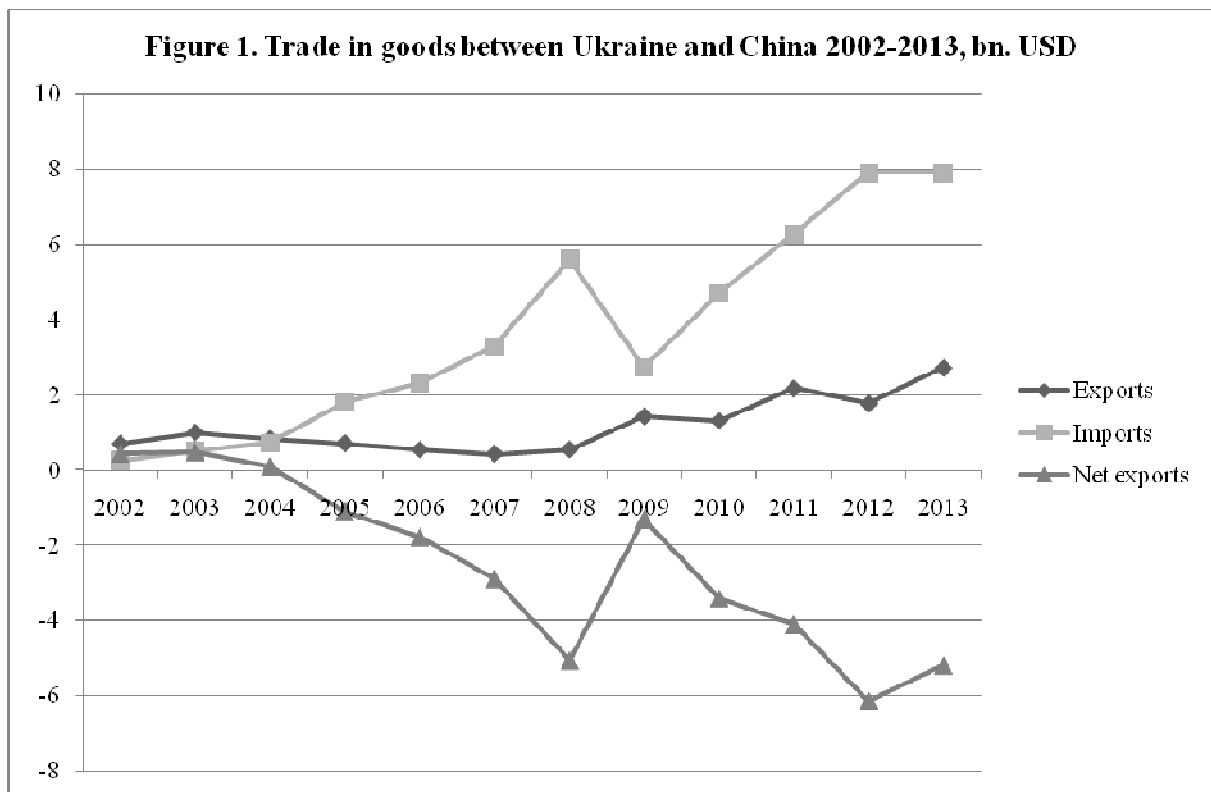
weaker impact on efficiency and competitiveness in Ukraine in comparison with China. The issue of inequity in China was analyzed in previous research (Kim 2013b), and the following research will show the efficiency of Chinese model and the comparative competitiveness with Ukraine.

However, the role of institutional instability in the formation of Ukrainian competitive advantages is considerable. In conditions of weak law enforcement and the robust import friendly foreign policy, most of national branches are unable to show high competitiveness and the efficiency of production. Especially it is common for export oriented and import replacing enterprises, which are directly compete with the world famous brands or the cheap products from China.

2. UKRAINE-CHINA TRADE COOPERATION

2.1. Trade imbalance growth between Ukraine and China

Figure 1 show the commodity imbalance, which appeared in 2005, after zero balance in 2004. And earlier, in 2002 and 2003 there were surplus in balance of trade in commodities because of Ukrainian exports excess over imports.



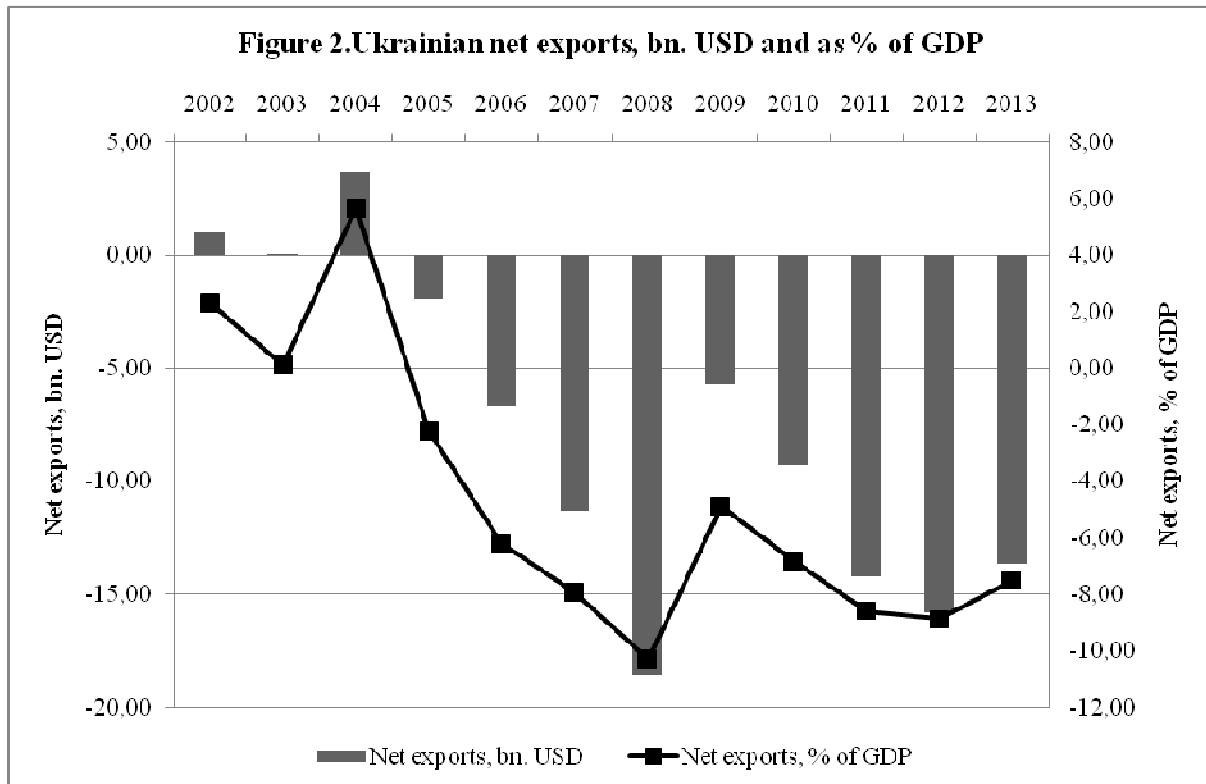
Source: <http://www.ukrstat.gov.ua/> (2014)

As it is shown on the Figure 1, the highest growth rates of imports from China to Ukraine were in 2007-2008 and 2009-2010. In fact, the imports value barely doubled both in those two periods, but during the 2009 year the rate of growth was negative and exceeded the rate of the previous period. So the level of imports was restored only in the period of 2010-2011. Ukrainian foreign trade is based not on international competitiveness of Ukrainian economy, but on the global market possibilities. On the other hand there are plenty of reasons for strengthening of Chinese commodities competitiveness, which were outlined by different researchers, Justin Yifu Lin (2014), and others. Among these reasons are: undervaluation of Renminbi Subramanian (2010), distortions in key industries, high income inequality, small share of domestic consumption of GDP in China. We may assume those factors to remain considerable in Ukrainian relations with China, like in the case with United States, described by Ghosh and Ramakrishnan (2012).

3. THE UKRAINIAN TRADE BALANCE

3.1. The Ukraine net exports

The US model of net exports shows correlation between the net exports volume and the share of net exports in GDP. Figure 2 shows Ukrainian trade balance in bn. USD and as % of GDP shows similar tendencies.



Source: <http://www.ukrstat.gov.ua/> (2014),

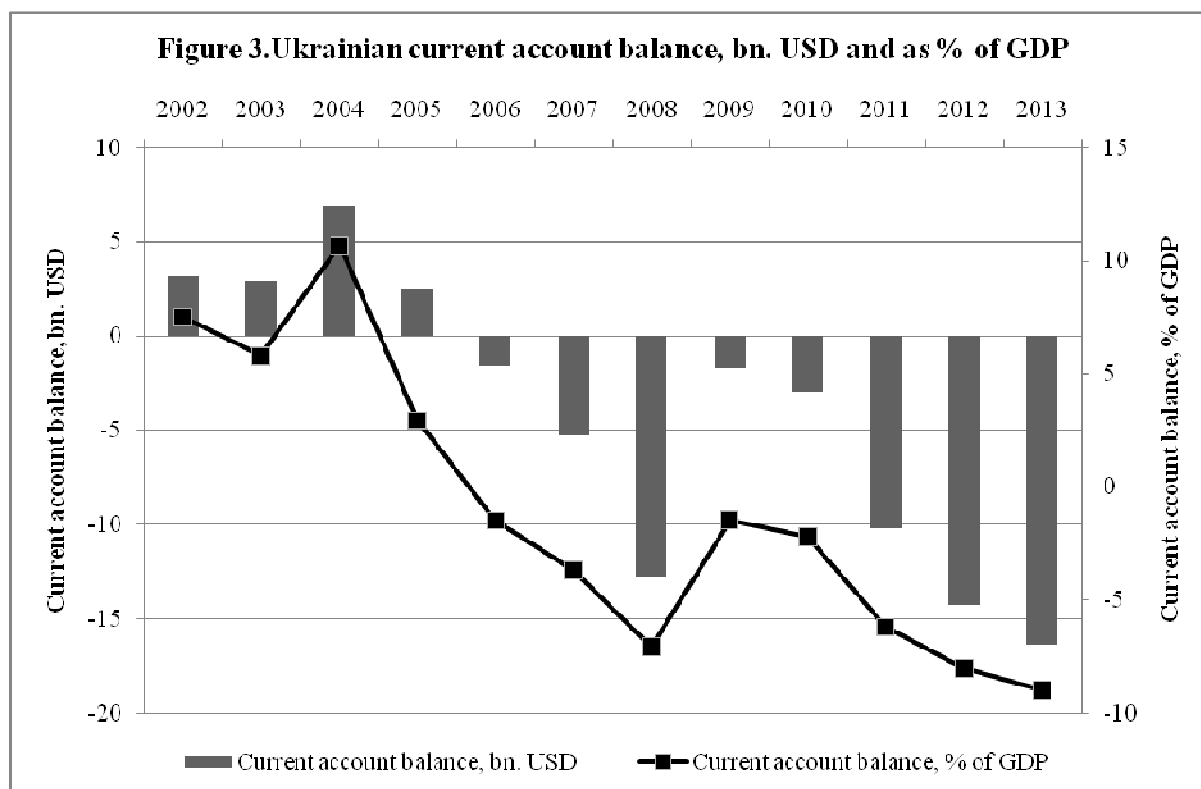
UNCTADSTAT, <http://unctadstat.unctad.org/TableViewer/tableView.aspx> (2012)

Since 2004 year the imports of base metals is showing the robust dynamics to growth, as it is shown in statistics (<http://www.ukrstat.gov.ua/> 2014). In 2004 it was equal to 1,75 bn. USD, in 2005 – 2,47 bn. USD (129,5 % of the trade deficit), in 2006 – 3,33 bn. (50 % of the trade deficit), in 2007 – 4,74 bn. (41,86 % of the trade deficit), in 2008 – 6,39 bn. (34,4 % of the trade deficit). In 2009 the imports of base metals decreased to 2,68 bn. (46,7 % of the trade deficit), in 2010 – 4,13 bn. (44,23 % of the trade deficit), in 2011 – 5,7 bn. (40 % of the trade deficit), in 2012 – 5,24 bn. (33 % of the trade deficit), in 2013 – 5 bn. (36,6 % of the trade deficit).

Ukrainian current account balance negative dynamics is shown on figure 3, but the deficit of current account appears in 2006, in difference with the net exports, and the amount of deficit is not as large as in trade of goods before the crisis. In 2008 the trade deficit was equal to -18,57 bn. USD, or 10,32 % of GDP, and the current account balance was equal 12,76 bn. USD, or 7,09 % of GDP.

3.2. Ukrainian current account balance

The trade deficit impact on current account balance is significant – the trade deficit is 413 % of the current account deficit in 2006, 215 % in 2007, 145 % in 2008, 331 % in 2009, 309 % in 2010, 139 % in 2011, 111 % in 2012 and 83,47 in 2013 year.



Source: <http://www.bank.gov.ua/doccatalog/document?id=63674> (2014).

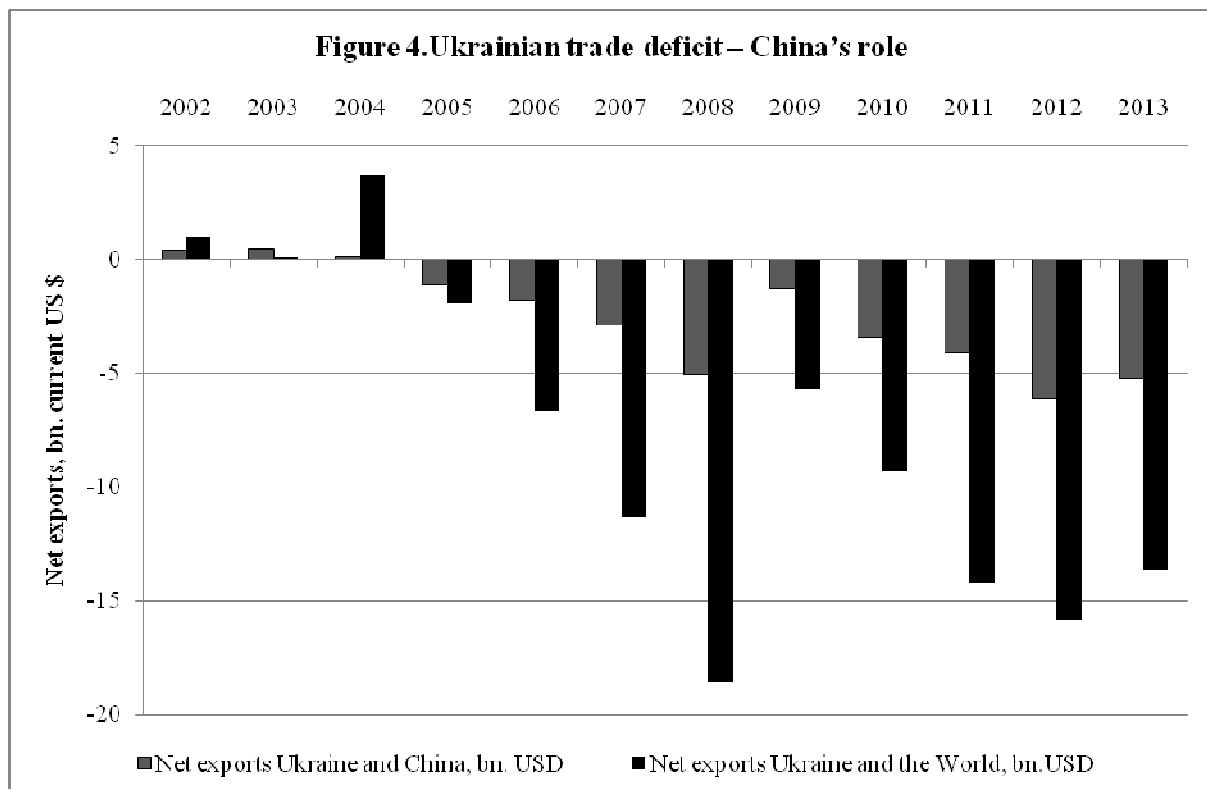
After the crisis the prevailing of trade deficit upon current account deficit remained until 2013, when the current account deficit exceeded the net exports deficit with 8,99 % of GDP (16,355 bn.USD) and 7,51 % of GDP (13,65 bn. USD). The explanation of this is decreasing of services balance surplus in 2013 from 5,15 to 4,11 bn.USD, increasing the balance deficit of primary income account from -2,96 to 3,02 bn. USD and decreasing of secondary income account from 2,98 to 2,15 bn. USD.

After all, in figures of National Bank of Ukraine, the net exports in 2013 decreased to -19,6 bn. USD, and it is the evidence of the inefficient foreign trade policy, that leads to inequality in foreign trade for the Ukraine.

Since 2005 China accumulates trade surpluses with the Ukraine (Figure 4). Those surpluses are sufficient for Ukraine – in its peak in 2005 the Chinese surplus achieved 57,6 % of Ukrainian deficit, in 2012 it was 38,6 % and in 2013 – 37,9 %. During the period of 2006-2013 the share of Chinese surplus changed in a range from 22,65 % in 2009 to 38,63 % in 2012.

4. THE IMPACT OF UKRAINIAN TRADE DEFICIT – CHINA’S ROLE

The China is one of the most important trade partners for the Ukraine for the last 5-6 years. In 2013 imports of goods from China is 10,26 % of the imports in the Ukraine, and exports to China is 4,31 % of the exports from the Ukraine.



Source: <http://www.ukrstat.gov.ua/>, (2014)

As a share of current account, the trade deficit with China has two peaks – 109,19 % in 2006 and 112,12 in 2010 with minimal value in 2013 – 31,64 %. Considering the issues of judging whether deficits are bad, as it is researched by Subramanian (2010) the analysis of savings and investments in the Ukraine showed the change in ratio of investments to savings since 2006 to 2012. In 2006 investments were equal to 283,3 % of savings, in 2007 – 394,5 %, in 2008 – 448,1 %, in 2009 – 188,8 %, in 2010 – 105,7 %, in 2011 – 193,4 %, in 2012 – 179,1 %. Also in 2013 the industrial indexes lowered to the average of 95 % from 100 % in 2012 and 108 % in 2011. Those figures are the evidence of extremely negative role of Ukrainian low competitiveness in trade with China and the necessity of strategy changing.

The change of foreign trade strategy must be grounded on the competitive advantages, as it was shown in previous study (Kim 2013a). The strategy of import substitution is the basis for current account surplus providing, which is strongly required for Ukrainian economy for the following 5-6 years during the period of IMF Stand-By Arrangement program – sited by IMF (2014). During this period building of the competitiveness basis in key industries and in national economy is essential challenge for this period. Efficient exploiting and development of national advantages, innovation strategy of economic development and rational current account managing are the key goals for public administration and resource allocation.

Creating robust competitiveness is the main goal for innovative strategy of import substitution of the Ukraine. The Ukrainian economy is one which uses rich natural resources, large scientific and technical base and human resources inefficiently. The economy, abundant with different resources must be highly competitive on the world market. This position will be provided with correct competitive strategy in both public and private sectors.

5. CONCLUSION

The paper explains the impact of the Ukraine and China international trade imbalance on the Ukrainian trade and current account deficit. The issue of Ukrainian industry international competitiveness is observed – the robust increase of the trade and current account deficit, as a result of China's international competitiveness strengthening over the Ukrainian is the crucial factor of economy development for the Ukraine.

If the Ukraine will continue implementation of the export orienting strategy, the international competitiveness of the economy will continue to degrade. Thus, the change of the foreign trade strategy is required: the innovative import substitution strategy, based on the competitive advantages creating and developing.

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