



DISCUSSION PAPER

COST-BENEFIT ANALYSIS

OPPORTUNITIES FOR THE EU
FROM UKRAINE'S ACCESSION

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COST-BENEFIT ANALYSIS: OPPORTUNITIES FOR THE EU FROM UKRAINE'S ACCESSION

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Introduction

Russia's full-scale invasion of Ukraine accelerated the country's European integration to the next level. From Ukraine's application for EU membership in February 2022 to the start of accession talks in June 2024, only two years have passed—a relatively short time for an EU candidate.

Despite the ongoing war, destruction, occupation of territory, population decline and other economic hardships, Ukraine's membership offers the EU certain opportunities, some of which may not be immediately apparent. This paper aims to initiate a discussion on these opportunities.

Ukraine's application for EU membership and the start of accession talks have sparked discussions on the costs and benefits for both sides. While studies suggest Ukraine's membership will lead to increased EU budget spending, these financial impacts are expected to be manageable. For Ukraine, EU integration offers the opportunity to strengthen democracy, modernize the economy, and aid post-war recovery. At the same time, Ukraine's membership would enhance the EU's global geopolitical role, fostering mutual benefits for both partners in terms of security, economic growth, and regional stability.

Ukraine has the potential to become a valuable partner for EU member states in key economic sectors. This paper analyzes the potential impacts of cooperation in agriculture, the pharmaceutical industry, energy, transport, and critical raw materials.

Ukraine's economy has demonstrated an unprecedented level of resilience to external shocks - given that it has been enduring war since 2014 (with intensity of hostilities varying across the decade), and even managing to develop. However, Ukraine's accession to the EU can offer mutual benefits, supporting Ukraine's post-war recovery while enhancing the EU's global competitiveness.

Ukraine's path to the EU: from the Association agreement to the membership negotiations

Since 2014, when the Association Agreement (AA) between the EU and Ukraine was signed and Russia started its aggressive war by occupying Crimea and invading Donbas, Ukraine underwent drastic changes in political and sectoral reforms. Due to the war, Ukraine lost eastern territories with their industrial capacity which caused trade reorientation and its structure. Ukraine became less dependent on the extractive industry and metallurgy and more reliant on services and agriculture. Over 2013 - 2021, the EU became Ukraine's main trade partner replacing the Commonwealth of Independent States (CIS), chiefly Russia. In fact, Ukraine did not completely reorient its trade from Russia to the EU; Ukraine still exported railway equipment to Russia, as there was no niche for this product in the EU market. Rather, Ukraine boosted the export of goods already present in the EU market and explored new opportunities provided by tariff liberalisation and lower non-tariff barriers under the AA.

The AA opened new trade opportunities for Ukraine, strengthened political ties between Ukraine and the EU, and paved the way for European integration reforms. For example,

Ukraine conducted reform of gas and electricity markets based on the EU's Third Energy Package, established anti-corruption institutional infrastructure, carried out public procurement reform, aligned with the EU's product safety requirements, implemented the EU legislation to accede to the common transit procedure (NCTS), reformed technical regulations in line with EU standards. Even though challenges remain and many reforms are yet to be made, Ukraine's European integration is already underway in many sectors. Thanks to the implementation of the AA, Ukraine has become familiar with the specifics of EU legislation and, thus, does not start the harmonization process from scratch. According to the self-screening conducted by the government, Ukraine is yet to implement around 3,000 EU legal acts. For comparison, the AA included around 500 legal acts and as of 2022, Ukraine implemented only less than half of them, according to the independent monitoring report.

At the same time Ukraine remains the poorest and the biggest country among candidate states. In 2023, its GDP per capita was 5,181.4 US dollars. This indicator grew compared to 2022 (4,576) but was due to the population decrease due to the war. Ukraine's GDP grew by 5-5.5% in 2023 which marked a recovery following a sharp 28.8% decline in 2022. Nevertheless, the current GDP remains about a quarter lower than in 2021. For comparison, the EU average GDP per capita in 2023 was 40,823.9 US dollars.

Such low numbers can be explained by the lingering effects of Russian aggression since 2014, a full-scale Russian invasion in 2022, and domestic factors such as inconsistent rule of law and weak protection of property rights that have hindered investment flows.

The war was a heavy blow to Ukraine's economy. As a result of Russian hostilities, 7% of Ukrainian territories were occupied, and the population is declining (a significant number of citizens lost their lives, some were deported or forcibly relocated to the aggressor country's territory, many Ukrainians emigrated, and the birth rate dropped drastically), a considerable part of the infrastructure was destroyed. As of January 2024, the total amount of damages caused to Ukraine's infrastructure due to the war stands at \$ 157 bln. As of the end of 2023, Ukraine's recovery and reconstruction needs are estimated at 486 billion US dollars.

Cost of integration

Therefore, Ukraine's application for EU membership and the start of the accession negotiations spurred discussion on the cost of Ukraine's accession to the EU, Ukraine's capacity to meet the Copenhagen Criteria, and Ukraine's economic potential as a candidate and future member state.

There are different studies on the cost of Ukraine's membership for the EU budget. An unpublished EU Council study (leaked to the media in October 2023) estimated that Ukraine's accession would cost €186 billion over seven years or €26 billion annually. According to these estimates, Ukraine's accession would incur considerable financial implications for the EU, "turning many existing member states from net beneficiaries into net payers". This study used the existing rules for the union's 2021-27 budget and applied them to an enlarged union including Ukraine, Moldova, Georgia and six western Balkan states. As per these estimations, the overall sum after adding nine new member states would amount to €256.8 billion which means that the current budget would increase by 21 per cent to €1.47tn. The study suggests that the accession of nine states would lead to significant financial adjustments - for example, farm subsidies for current member states would be reduced by approximately 20 per cent and cohesion funding would no longer be available to the Czech Republic, Estonia, Lithuania,

Slovenia, Cyprus, and Malta. However, the results of this report were questioned by various analysts who provided different figures.

For example, Bruegel's report suggests that the net cost of Ukraine's EU membership at current prices in total in 2021-2027 would amount to € 137 bln (provided that Ukraine restores its territorial integrity and sustainable development of the economy and population), which is 0.13 per cent of EU27 GDP, or € 110 bln (if Ukraine loses 20% of agricultural land and the population and GDP continues to decrease), which is 0.10 per cent of EU27 GDP. For comparison, after the 'big bang' enlargement, concerning the GDP of the old Member States (EU15), total transfers from the EU budget to the new Member States were 0.2% in 2007 and rose to 0.3% by 2013. These transfers accounted for approximately 2% of the GDP of new Member States in 2007 and increased to 3% by 2013. This comparison allows us to assume that even if Ukraine's accession brings an increase in the EU budget, it will remain bearable for the current EU member states.

According to Michael Emerson's paper, Ukraine would benefit from around EUR 18-19 billion of receipts from the EU budget, if it hypothetically joined the EU today with current parameters of GNI, population, land area, etc. At current rates, this would result in an approximate 10% increase in GNI-based contributions from all Member States, with only Spain shifting from a (small) net beneficiary to a (small) net contributor. This would not change the position of Member States that acceded from 2004 on, as they would still remain considerable net beneficiaries.

According to the calculations of Hertie School - Jacques Delors Centre "in a hypothetical scenario applying the data and budgetary rules of 2021, no member state would turn from net beneficiary to net contributor if Ukraine joined. The accession of Ukraine, Moldova, Bosnia and Herzegovina, North Macedonia, Montenegro, Albania, and Serbia would result in total annual additional spending of about 19 billion Euros, i.e. a bit more than 10% of the current budget which would still lie under the EU's current own resource ceiling of 1.40 percent of EU GNI." As for Ukraine alone, "the annual additional spending for the EU under a Ukrainian accession would amount to 13.2 billion Euros."

In a nutshell, Ukraine's membership will inevitably lead to an increase in the EU budget spending and impact the distribution of funding under the common agricultural and cohesion policies. However, as several studies showed, it would hardly turn many EU member states from net receivers into net payers. At the same time, these assessments are just hypothetical for at least two reasons. Firstly, the war makes it difficult to predict the state of Ukraine's economy at the time of accession. Secondly, the rules and allocations under the EU's Multiannual Financial Framework (MFF) are always subject to political negotiations, and it is therefore difficult to predict what the MFF will look like when enlargement takes place.

When it comes to the size of Ukraine's economy and wealth, it is comparable to the Central, East and South-eastern European (CESEE) states when they applied for EU membership in the 1990s. Ukraine's economy is approximately 1% the size of the EU-27 economy, which is almost at the same level as Hungary's or Romania's economies were relative to the then-EU-15 before their EU accession in 2004. Regarding wealth (GDP per capita at purchasing power parity), Ukraine is roughly comparable to the poorest CESEE countries, Latvia and Romania, at the time of their membership application. However, Ukraine is much poorer than current accession hopefuls (except Kosovo and Moldova), and the poorest among countries at the time of their accession to the EU. Nevertheless, the example of the poorest former CESEE candidate states shows that further integration with the EU boosts catch-up economic growth (Romania is a case in point).

In the case of Ukraine, such catch-up gains may result from capital inflows from post-war reconstruction, Ukraine's potential in different sectors, and EU technical assistance for Ukraine's governance reforms. The latter aspect is crucial as it is key to ensuring an enabling environment for economic growth and private capital inflows. Ukraine starts its accession

negotiations with a much weaker institutional environment than CESEE states did, and therefore Ukraine should reform significantly quicker. Studies suggest that if Ukraine reforms with the same speed as the CESEE joiners did it will reach the level of Romania at the time of its accession (theoretically minimal level for accession) only in 2032. It means that Ukraine has a tense reform agenda ahead. The EU can play a significant role by providing technical assistance and monitoring reform progress.

European integration of Ukraine would bring opportunities for both partners, Ukraine and the EU. For Ukraine, it is about strengthening democracy and the rule of law, modernising the economy and post-war recovery. While Ukraine would strengthen the EU in many sectors, making it a stronger global actor.

Sectoral dimension

Experts identified the following sectors where Ukraine can strengthen the EU: agriculture, energy sector, transport, and critical raw materials.

Agriculture is one of the most complicated sectors for EU integration negotiations. Ukraine ranks top 10 among producers of sunflower, sunflower oil, corn, wheat, barley and rapeseed worldwide. Most of the Ukrainian harvests are exported. Though the EU's single market is the biggest export market for Ukraine (7.7 bln. USD in 2021), aggregate amounts of exports to all third countries is significantly higher (more than 20 bln USD). Indeed, due to the war and Black Sea blockade in 2022 agrarian exports to the EU substantially increased, but now Ukraine is trying to recapture its traditional markets.

Some Member States fear potential competition from the Ukrainian agrarian sector. One of their main concerns is the high amount of subsidies Ukraine's agriculture may be eligible for under the CAP. However, previous experience of the EU enlargement shows that CAP underwent significant reforms before new members' accession (such as Spain's accession case and CEE countries' accession, where CAP has been altered to ensure that "old" member states may enjoy the same level of support).

In the meantime, Ukraine's accession creates several significant opportunities for the EU.

- **Commercial leadership in agricultural trade.** The EU can become a world-leading producer of certain agriculture products after Ukraine's accession, thus increasing the revenues for the whole bloc.
- **Supply chain cooperation.** There is also strong potential for cooperation between Ukrainian grain producers and European livestock and food producers, enabling the expansion of EU-made meat and poultry for the third markets.
- **Food security.** Ukraine's accession would bolster EU food security, as EU producers (e.g. livestock farming) would enhance access to Ukrainian feed grain and vegetable protein meals. Additionally, Ukraine's fertile soils would become an integral part of the EU's soil resources.
- **Food sovereignty.** Ukraine has traditionally competed with Russia in supplying wheat, rapeseed oil and rapeseed meal to the EU markets. Integration of Ukraine into the EU would strengthen the EU's resilience against Russian threats.

- **Political leadership.** Given that Ukraine is also an essential supplier of food for Global South countries, Ukraine's joining the EU will increase the political and economic influence of the EU in this region. By joining the EU, Ukraine would help the bloc secure a leading position in the export of crops and oils, providing an opportunity to diminish Russian presence in African markets and reduce its influence there.
- **Green agriculture.** Ukraine's agriculture could also support the EU's transition to greener farming practices, as pesticide and mineral fertilizer usage in Ukraine is significantly lower than the EU average.

The **pharmaceutical industry** is a very important industry for the Ukrainian economy (though constituting only 0,7% of GDP in 2021). The COVID-19 pandemic and the Russia-Ukrainian war showed a big importance of the country's ability solely to provide its population with medicines. As for 2023, Ukrainian manufacture of pharmaceuticals is domestically oriented (63,4% of products are destined for the Ukrainian market). The export of pharmaceutical products is only 0,8% of all Ukrainian exports in 2023. The leading importers of Ukrainian pharmaceuticals are Uzbekistan, Kazakhstan, Georgia and Moldova. Lithuania is the only EU country among the most important importers of Ukrainian pharma.

The main obstacle for Ukrainian pharmaceutical exports to the EU is non-tariff barriers. To fully access these markets, the EU needs to recognize Ukrainian GMP (Good Manufacturing Practice) certificates. Mutual recognition of GMP certificates between the EU and Ukraine could significantly boost trade in the pharmaceutical sector.

The COVID-19 pandemic highlighted the EU's heavy reliance on India and China for certain pharmaceutical products - due to the relocation of production to Asia and the resulting scarcity of production sites in Europe. As dependency on drug supply is a challenge for the Union's security, the Ukrainian pharmaceutical industry has the potential to become a supplier of generic drugs and active pharmaceutical ingredients (APIs), helping the EU reduce its dependency on long supply chains from India and China.

The **energy** sector in Ukraine before the war was diverse and met all the needs of energy consumption of the country. However, the ongoing war-related destruction and regular missile attacks on the energy infrastructure significantly deteriorated Ukraine's energy system and made consumers vulnerable to electricity supply shocks. Ukraine lost the Kakhovka Hydro Power Plant (HPP), Dniprovsk HPP was severely damaged, most of the thermal power plants also were damaged or destroyed, and the biggest nuclear power plant (NPP) in Europe - Zaporizhzhia NPP - is occupied. For this moment Ukraine's energy sector is highly dependent on the EU's support.

In the mid-term Ukraine can offer several advantages to the EU energy sector:

- **Green energy.** Ukraine has significant potential for renewable energy, including solar, wind, and biomass. The unique climate conditions in southern Ukraine, compared to other Central and Eastern European countries, offer distinct opportunities to expand the share of renewable energy sources (RES) in the EU's electricity generation.
- **Green gases.** Ukraine also holds strong potential for green gas production, including biomethane and hydrogen. However, realizing these projects currently requires foreign investment.
- **Regional energy security.** Ukraine's integration into the ENTSO-E can enhance regional energy security by creating a more balanced regional energy market. However, new interconnections between Ukraine and its neighbouring countries will need to be established.
- **Gas sovereignty.** Ukraine's extensive gas storage facilities can be utilized by other EU Member States to bolster sovereignty in the gas market.

- **Energy resilience.** Ukraine has unparalleled experience in protecting power plants and energy infrastructure. This expertise can be invaluable for the EU's security and energy sovereignty.

Transport is a very important sector that provides connectivity and trade. Logistics networks are also a vital part of national security. The main issue in Ukraine's transport sector is the poor quality of transport infrastructure. The ongoing war has considerably worsened the situation due to the damages reaching approximately USD 33.6 bn, including the destruction of 25,000 km of roads and 344 bridges.

Ukraine also still has to adapt its legislation in the transport sector in line with EU acquis.

Opportunities for the EU in the transport sector through Ukraine's accession:

- **Trade facilitation.** Ukraine's accession to the EU will spur the development of new transport routes, enhancing cross-border trade. For example, Ukraine has begun exporting agricultural products through Romania's Port of Constanța, leading to increased investments in the port and its operators.
- **Sustainable transportation:** Integrating Ukraine's railway infrastructure with the European network will boost rail transportation of goods and passengers. Since rail transport is significantly more environmentally friendly than road transport, this will contribute to greener logistics. Ukraine has already initiated relevant infrastructure projects, such as the development of the 1435 mm track on the Chop-Lviv and Lviv-Chernivtsi-Vadul-Siret-state border sections. Additionally, enhancing transport routes along the Danube River will further promote environmentally sustainable goods transportation.

Critical raw materials. Ukraine can contribute to the EU's green transition as a supplier of critical raw materials. Ukraine possesses deposits of gallium, rutile, titanium sponge, graphite, magnesium ores, lithium and other important green transition minerals. These resources can boost the production of green products in the EU and reduce the dependency on China.

Unfortunately, some of these deposits are located in the occupied regions or territories with ongoing hostilities. For example, the biggest Ukrainian producer of neon gas, which is critical for semiconductor chips, is located in occupied Mariupol.

In 2021, the EU and Ukraine signed a strategic partnership on raw materials as part of a broader initiative to reduce the Union's dependence on China for essential raw materials.

In the post-war period, Ukraine will be able to start projects for the extraction of critical materials, but it is essential to implement environmentally friendly technologies to avoid further harming the already war-affected environment.

Conclusions

European policymakers should consider Ukraine's accession to the EU not as a challenge but as an opportunity. The Russian invasion blew up Ukraine's weak economy. Still, further EU integration may be a chance for Ukraine to conduct reforms and attract investments. As the example of the CEE countries shows, EU membership significantly boosts economic growth. Apart from the sectoral reforms, Ukraine also needs to strengthen the rule of law in order to ensure an enabling environment for the functioning of the market economy and investment inflow.

Even though Ukraine's accession will lead to an increase in the EU budget, the benefits of Ukraine's accession are much bigger. Ukraine remains a competitive actor in agriculture, and thus Ukraine's accession would create an opportunity for the EU to become a world-leading agricultural producer and would contribute to the EU food sovereignty and security. In the sector of pharmacy, Ukraine has the potential to replace China and India in the supply of generic drugs and active pharmaceutical ingredients and thus reduce the EU's dependency on supply from Asia. The Ukrainian energy sector has experienced severe suffering from the Russian missile strikes, however, Ukraine's experience in protecting its energy infrastructure is valuable to ensure the EU's energy resilience. In addition, Ukraine has the potential to develop green energy and produce green products which can help the EU boost its green agenda on the international level. The transport sector has also suffered from the war repercussions, however, the EU may assist Ukraine in developing transport roads and integrate Ukrainian railways with European networks to enhance cross-border and sustainable transportation.

Recommendations for the EU

1. The EU should consider supporting Ukraine in its governance reforms (especially public administration reform).
2. Initiate discussions on adapting the Common Agricultural Policy (CAP) in preparation for the accession of new member states, including Ukraine.
3. Consider Ukraine as a partner in agriculture rather than a competitor. Given Ukraine's significant role in supplying animal feed, enhance collaboration between Ukrainian grain producers and European livestock farmers and food producers.
4. Consider integrating Ukraine's pharmaceutical industry into the EU market through a Mutual Recognition Agreement of Good Manufacturing Practice (GMP) certificates between the EU and Ukraine. This cooperation will help reduce the EU's dependency on long supply chains from India and China.
5. Support renewables and green gas projects in Ukraine, which holds significant potential for development in these areas. Ukraine's contribution can greatly enhance the EU's green energy transition efforts.
6. Promote integration/interconnection enhancement of Ukraine's transport infrastructure with the EU, focusing on sustainable cross-border connectivity. Prioritize development of new transport routes (including rail networks), and environmentally friendly logistics to facilitate trade and reduce carbon emissions.
7. Enhance Ukraine's integration into EU supply chains as a supplier of critical raw materials. This will reduce dependency on China and Russia while supporting the EU's green transition and boosting the set-up of relevant industries in Ukraine.



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