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**Impact of joining the WTO on Ukrainian ferrous metallurgy:
subsidies vs. antidumping, is there really a trade-off?**

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Abstract

Authors provide a case study of the impact of antidumping and subsidies in Ukrainian steel. They argue that that accession the WTO for Ukraine will require the elimination of subsidies to Ukrainian steel. This will result in a benefit to Ukraine in a decline in antidumping actions against Ukrainian steel in its export markets. The authors quantify the impacts. Contrary to popular discussion in Ukraine, they show that the reduction in subsidies in Ukraine will also benefit the country as a whole. So, despite losses to the producers of steel, accession to the WTO, which entails both subsidy reduction and reduced antidumping against its exports, should be a win-win situation for Ukraine.

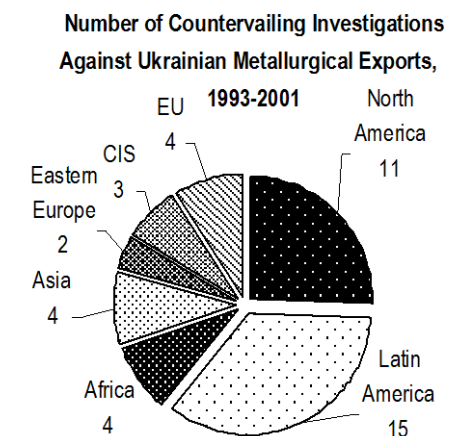
Sector, discussed most hotly in connection with possible Ukraine's membership in the WTO, is probably metallurgy. Opinions differ diametrically opposite, from hopes that the WTO will help Ukraine to develop the sector and obtain larger share of the world market to fears that metallurgy will not be able to compete equally and will cease. Such reaction is not surprising, taking into account size and importance of the metallurgy for Ukrainian economy. Ukraine is the 7th biggest steel producer and 4th biggest steel exporter in the world. The sector employs more than 500 thousand workers; its share in total industrial production is around 28%, while share of metallurgy in Ukrainian exports is around 50%.

Ferrous metallurgy sector was traditionally considered to be strategically important for Ukraine and at all times received one or another form of support from the state. At the first half of

1990's government granted to metallurgical enterprises various subsidies, tax exemptions and other privileges. In 1999 government of Ukraine adopted program of state support for metallurgy. Among the privileges, the largest one is reduced enterprise profit tax (EPT). Tax rate for participating enterprises was set at the level of 30% of general tax rate. Thus, instead of existing EPT rate of 30% metallurgical enterprises enjoyed 9%. Later on EPT rate for metallurgical companies was set at the level of 15%. Other privileges include eliminated roads fund fee, reduced innovation fund fee (50% of general rate), reduced fee for environmental pollution, write-off of all fines for delay of tax payments prior to July 1999; after July 1999 reduced rate (50%) for fines apply.

In 2002 the Cabinet of Ministers worked-out program of the metallurgical sector development till 2010. According to this program, the state will continue granting tax privileges to the metallurgical companies and even may grant direct transfers of public funds to the sector.

Existing program of state support contradicts GATT/WTO requirements, particularly Article I 1.1 a) (ii) – subsidies and compensation and Article III.2 – national regime of domestic taxation. Not surprisingly, Ukrainian ferrous metallurgy companies faced increasing number of antidumping investigations, while government support was one of the major reasons for filing the suites.



Source: Ministry of Economy of Ukraine

Between 1993 and 2001 there were initiated 43 cases of countervailing investigations against Ukrainian ferrous metallurgy. As can be seen from the graph, the major countries, which initiated investigations, were in Latin America and North America (15 and 11 cases correspondingly), followed by Asia, Africa and EU. Size of countervailing duty varied considerably from case to case: from 9% to 96%.

It is stated that If Ukraine is to join the WTO, there will be a trade-off: Ukraine will have to abandon subsidies (which are claimed to have substantial positive impact on industry growth), but at the same time will be able to fight against antidumping (“unfair” pricing) duties and especially against countervailing (“unfair” subsidies) duties. In order to check such statement partial equilibrium model was developed, which study effect of both cases and allows to find net impact on metallurgy and total welfare. Our calculations were done for year 2000.

Results of the model are shown in the table below, negative number means loss, while positive shows gain:

	Effect of canceling subsidies	Effect of reducing antidumping	Total effect
Producers	- USD 287 m	USD 92 m	- USD 195 m
Consumers	- USD 30 m	- USD 10 m	- USD 40 m
Government	USD 578 m		USD 578 m
Total	USD 261 m	USD 82 m	USD 343 m

Our calculations show that steel producers will lose profits after the subsidies are cancelled; but Ukrainian steel exports will benefit from the reduction in antidumping investigations and lower antidumping duties against Ukrainian exports. Besides that, gains from subsidies in the long run are by far less sustainable than gains from the competitive development of an industry. Producers themselves are interested in competitive environment, since developing truly efficient production will give higher profits over the long run and allow to compete at international markets. Maintaining inefficient and maybe profit-making production by subsidies on opposite just waists money without making production any more competitive. Moreover, Ukrainian metallurgy makes intensive use of intermediate goods, first of all energy, imported from Russia (energy amounts to 30% of production costs). Hence, subsidies to Ukrainian steel producers anyway are partially shifted to foreign suppliers of intermediate good.

Domestic consumers will experience small welfare losses as a result of higher prices for steel products. The biggest gains will accrue to the government budget, which will benefit from the reduction in subsidies. This surplus can be distributed back to the consumers by government to make former better off. On balance the total gains for the Ukrainian economy are calculated to be above USD 343 million, or 1.1 % of GDP.

To sum up, we see that in subsidies-antidumping duel there is no trade-off for the Ukrainian economy taken as a whole. It is widely recognized that by eliminating subsidies, Ukrainian steel exports will face fewer antidumping suits which will have a positive effect on Ukrainian exports and the price received by Ukrainian exporters of steel. Besides that, equal conditions will allow to promote development of competitive production. Further, elimination of subsidies is also beneficial for the whole Ukrainian economy. The Ukrainian government will save a substantial amount of money by canceling subsidization. It should be noted that it is very important to insure channeling those funds to more productive needs, such as investing in human

and physical capital, developing infrastructure, etc, but not to enlarging bureaucratic apparatus or increasing military expenditures. Benefits from decreasing antidumping investigations, more competitive production and better use of budget funds exceed the losses of the producers and the small losses of consumers of steel. Thus, our study shows that Ukrainian economy will benefit from free trade and accession to the WTO should be set as the priority goal of the external policy. Ukrainian government will make a favor to everyone by changing hesitations to active policy of promoting WTO membership.