

Trade liberalization gains under different trade theories: A case study for Ukraine

To analyze the Deep and Comprehensive Free Trade Area (DCFTA) between Ukraine and the EU we develop a multi-region general-equilibrium simulation model calibrated to GTAP 8.1 data. We implement three alternative trade structures for services and manufactured goods: a.) a standard specification of perfect competition based on the Armington [1969] assumption of regionally differentiated goods; b.) monopolistic competition among symmetric firms consistent with Krugman [1980]; and c.) a competitive selection model of heterogeneous firms consistent with Melitz [2003]. Across these structures the DCFTA indicates relatively large gains for Ukraine (and small gains for the EU). A novel result emerges, however, in that the gains for Ukraine are largest under an assumed Armington structure. This is attributed to a movement of resources into Ukraine's traditional export sectors which produce under constant returns. While there is little danger of deindustrialization dominating the overall welfare gains, we do observe substantially lower gains due to monopolistic competition.