

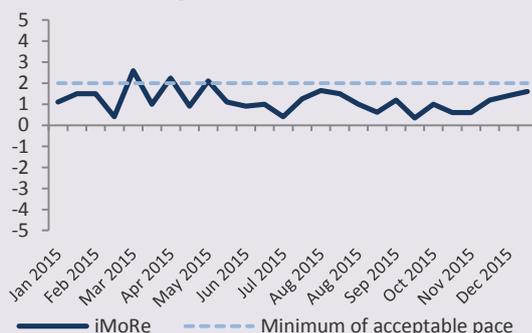
Economic reforms in Ukraine— Moving forward slowly

The Index for Monitoring Reforms (iMoRe) evaluates changes in Ukraine’s legislation. The index suggests that economic reforms in the country are moving forward, but the progress remains slow and partially owes to pressure from the international community. The most important achievements since early 2015 include an IMF-required sharp hike in energy prices, a legislative act strengthening bank owner liability, the introduction of an electronic public procurement system, the launch of the national police as well as a set of initiatives aimed at increasing transparency and deregulating the business environment. Proper implementation of progressive legislation remains an important impediment. Cases of successful implementation represent only a fraction of the wide reform agenda Ukraine faces.

Economic reforms: Moving forward slowly

It’s been almost a year since the Index for Monitoring Reforms (iMoRe) was launched by VoxUkraine, a group of Ukrainian economists. The index measures the legislative aspect of Ukraine’s reform process. About 30 experts participate in a bi-weekly survey evaluating the potential impact of adopted laws and other legislative acts on the scale from -5 to +5 over five spheres: (1) governance and anti-corruption, (2) public finance, (3) monetary policy and financial markets, (4) industrial organisation and foreign trade, and (5) energy independence.

Index for Monitoring Reforms



Source: VoxUkraine

The result of this regular monitoring leaves a mixed impression about Ukraine’s economic reforms. On a positive note, the index never slipped into negative territory (see figure above) and only five out of over 300 legislative acts were rated negatively. This suggests that economic reforms are moving forward - at least as far as legislative changes are concerned.

On the other hand, on only three occasions the index was higher than +2.0 – a level that its creators consider to represent an acceptable pace of reforms. In all of

these cases, the underlying legislative changes were adopted to meet the requirements of the IMF and other international financial institutions in the framework of the USD 25 bn support package.

Thus, Ukraine is moving forward on the way of economic reforms, but the progress remains slow and is partially pushed from the outside, i.e. by the IMF and other official creditors.

Milestones in legislation

In addition to assessing reform progress in five directions, experts evaluate the potential impact of each individual piece of legislation under the implicit assumption of the latter being implemented in due course. Out of more than 300 legislative acts assessed since early 2015, the highest scores were assigned to the government’s decisions to sharply raise household gas tariffs, the approval of legislation introducing an electronic system for public procurement and the approval of the law strengthening the liability of banks’ owners (see table below).

Legislative acts with highest iMoRe scores

Type of reform	Score
Hike in gas tariffs for households	9.0
Public procurement legislation	8.5
Law increasing liability of banks’ owners	7.0
Gas market law	6.8
Changes to joint stock company law	6.0

Source: VoxUkraine

The government’s decision to raise household gas tariffs by 3-5 times in April 2015, thus raising them towards the cost-covering level, was assessed by iMoRe experts as the most important reform (9.0 points). The IMF-required hike (accompanied by subsidies for low income households) reduced huge distortions in the energy market, thereby significantly strengthening Ukraine’s fiscal position, decreased corruption opportunities and introduced incentives for energy saving. The approval of the law "On natural gas market", which introduced the regulatory principles of the EU and opened the gas market for competition, represents another milestone in the energy sector.

The legislation introducing an electronic system for public procurement was considered the second most important reform (8.5 points). This reform will enable switching from current ineffective procurement procedures, prone to manipulations, to the fully transparent electronic system called *ProZorro* that allows free competition and eliminates corruption opportunities. Potential annual savings from the usage of this electronic procurement system for all purchases are esti-

mated to amount to UAH 50 bn (about 2.5% of GDP) per year.

The law to increase the liability of banks' owners – another IMF-required piece of legislation – received the third highest score (7 points). Inter alia, this law foresees criminal responsibility of banks' owners in case of bankrupting a bank if losses exceed a certain, relatively small amount.

There were also several important initiatives aimed at increasing transparency of the state such as an online system gathering all state budget transactions (*e-data project*) and the opening of more than 300 government registers and data bases. High scores were assigned to the introduction of the national police that substituted soviet-style militia, the introduction of online administrative services for business by the Ministry of Justice as well as a set of initiatives deregulating the business environment.

Implementation remains a key issue

Despite some progress in reforms, including initiatives aimed at fighting corruption, the general public does not feel satisfied. According to the November 2015 survey by the International Republican Institute, only 15% of Ukrainians believe the country is heading in the right direction. Earlier surveys by the same organisation revealed that Ukrainians support reforms, but they are frustrated over the lack of progress in their implementation.

The same conclusion can be drawn by taking a closer look at the legislations that received the highest scores based on the iMoRe methodology.

One starting example is the law to increase the liability of banks' owners that was enacted back in March 2015. Since the ongoing economic crisis started, more than 60 banks out of 180 were sent into receivership, and rehabilitating the banking system has cost the state 3.7% of GDP. However, there was not a single legal case opened against the owners of bankrupted banks.

Another example is the law "On natural gas market" aimed at opening the domestic gas market to competition. Though the law was adopted in April and enacted in September 2015, necessary implementation provisions, i.e. complementary "sublegal acts", were published only in November 2015. Furthermore, according to an official from the state-owned oil and gas monopoly Naftogaz, those sublegal acts contradict the spirit of the law and are likely to limit competition in the gas market.

For the sake of fairness, it should be noted that there are examples of successfully implemented reforms. This list includes the hike in energy tariffs, the gradual switch to the electronic public procurement, the business deregulation and the introduction of the national police. The energy tariff hike was politically hard to adopt, but, after making a political decision, imple-

mentation became a purely technical issue. On the contrary, the implementation of the police reform required much effort and determination from the side of Georgian and Ukrainian enthusiasts. However, these successes represent only a fraction of a wide reform agenda that Ukraine faces.

Conclusion

The opposition to reforms in Ukraine is strong and originates from many sources – oligarchs, state bureaucracy, and the vast majority of people used to "traditional" ways of doing things. However, reforms are moving forward fostered by the pressure created by the international community and the local civil society. Given a mix of widespread vested interests and a developing democracy, we can hardly expect Ukraine to become another "breakthrough" reformer similar to Georgia or Singapore. Rather, changes will arise as a result of systemic step-by-step effort, but will go hand in hand with changes in the mentality of the society implying a smaller probability of reversal of reforms.

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Founded by foreign and local economists and lawyers, VoxUkraine (www.voxukraine.org) seeks to provide an independent, high-quality, research-based policy analysis and discussion platform on an international scale monitoring Ukraine's reform process. Olena Bilan and Ilona Sologoub are members of its editorial board and founders of the iMoRe project.

Note: This text is the sole responsibility of the authors and does not necessarily reflect the opinion of the German Advisory Group.

German Advisory Group

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