

# BTI 2016 | Ukraine Country Report

|                          |       |             |             |       |
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This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2016. It covers the period from 1 February 2013 to 31 January 2015. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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**Key Indicators**

|                          |        |      |                                |       |                      |        |
|--------------------------|--------|------|--------------------------------|-------|----------------------|--------|
| Population               | M      | 45.4 | HDI                            | 0.734 | GDP p.c., PPP \$     | 8665.5 |
| Pop. growth <sup>1</sup> | % p.a. | -0.3 | HDI rank of 187                | 83    | Gini Index           | 24.6   |
| Life expectancy          | years  | 71.2 | UN Education Index             | 0.796 | Poverty <sup>3</sup> | % 0.1  |
| Urban population         | %      | 69.5 | Gender inequality <sup>2</sup> | 0.326 | Aid per capita \$    | 17.6   |

Sources (as of October 2015): The World Bank, World Development Indicators 2015 | UNDP, Human Development Report 2014. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.10 a day at 2011 international prices.

## Executive Summary

The period under review saw a fundamental and, in many aspects, even revolutionary change in Ukraine. On the one hand, these changes opened up prospects for true democratization but on the other, they led to the loss of a part of the country, Crimea, annexed by Russia, and a war in eastern Ukraine fueled by Russia and its military involvement.

During most of 2013, Yanukovich was preparing to win a second term through elections scheduled for early 2015. To this end, he put the judiciary, law-enforcement apparatus, civil service and other public resources and institutions under his control and the control of the so-called “family” – a narrow group of people close to him and his son Oleksandr. Media freedom was curtailed and freedom of assembly was significantly limited. Nevertheless, Yanukovich was showing willingness to sign the Association Agreement with the EU and avoided being dragged into the Eurasian Economic Union.

When, at the very last minute, preparations for signing the Association Agreement were suspended, civil society activists and students took to the streets. After the Berkut special police unit brutally dispersed the protesters, leaving dozens of protesters heavily injured or missing, hundreds of thousands of people turned up. As the authorities continued in their attempts to disperse protesters with police forces and banned protests, more people took to the streets, barricades were erected and the protest movement radicalized.

The protests and the reaction of the authorities revealed two important developments in Ukraine. First, it became clear that Yanukovich had de facto privatized the state. Second, civil society in Ukraine had matured and become capable of organizing infrastructure that supported the Euromaidan. Moreover, the Euromaidan revealed the high degree of social capital that had emerged in Ukraine. According to one public opinion poll, about 20% of Ukraine’s population

was involved in protests in some way. Protests also took place throughout Ukraine, including regions where the Russian language dominated.

The Euromaidan ended on 22 February 2014, with more than 100 people dead. At the same time, amendments to the constitution that provided for power sharing between the president and the parliament/prime minister were adopted. Yanukovich fled Ukraine and a new transitional government was appointed.

In May and October 2014, early presidential and parliamentary elections took place. Both elections were free and fair. Thus, the key branches of power have gained the legitimacy they lost during Yanukovich's presidency.

Reform has also progressed, although slower than expected. The parliament passed important laws that paved the way for reducing corruption, launching public broadcasting, lustration, transparency, decentralization and other important initiatives, but their implementation has been uneven.

Importantly, civil society in Ukraine is now much stronger than before and keeps exercising pressure on the authorities. This, coupled with the fact that many civil society activists, experts and business managers became members of parliament or took positions in the government, provides some grounds for optimism.

These processes are taking place in difficult circumstances. First, Ukraine is in a deep economic crisis. High level of indebtedness, a fragile banking system, balance of payments imbalances as well as declining production and military conflict pose serious risks for the state. Comprehensive structural reforms are to be coupled with urgent macroeconomic stabilization.

Second, Russia intervened militarily, annexing Crimea and occupying parts of the Donetsk and Luhansk regions (Donbass). This proxy war has led to large-scale destruction. According to the United Nations and OSCE, by May 2015, over 6,000 people had been killed (both military and civilians), while more than 1.5 million had become internally displaced. Millions of people are still staying in the zone of military action, many of them in need of humanitarian assistance.

While this creates a tremendous challenge for the state, this has also provoked a consolidation of Ukrainian society. The unprecedented growth of volunteering has, in many cases, served as a substitute for the weak and even dysfunctional state. According to opinion polls, over 70% of people in Ukraine have either become volunteers or have donated support to the army and those in need.

## History and Characteristics of Transformation

Until 2014, Ukraine's post-independence transformation was largely determined by old nomenklatura elite groups who kept their positions in the state administration and the economy after 1991. They shaped the new institutional framework according to their own interests, relinquishing conflict-laden economic policies, avoiding any difficulties for themselves and failing to act in concert because of internal competition for wealth and power. At the same time, new opportunities for individual and group enrichment such as rent-seeking emerged and were partially sustained by international – Western and Russian – support.

From 1996 until 2005, Ukraine was formally a semi-presidential system. Leonid Kuchma's second term (1999 – 2004) was characterized by increasing authoritarian tendencies and informal power relations. Various protests against his regime galvanized opposition movements which finally led to the Orange Revolution. This occurred at the end of 2004, triggered by fraudulent presidential elections. The key demand of the protesters - free and fair elections - was realized.

The inauguration of Viktor Yushchenko as president in January 2005 and the parliamentary approval of Yulia Tymoshenko's candidature as prime minister in February 2005 marked a significant shift in power. However, few of the expectations and promises (more democracy, transparency and socioeconomic change) were realized, and public disillusionment ensued.

During the "Orange" period between the 2004 and 2010 presidential elections, most Ukrainian governments suffered from internal disunity and constant competition for power, facilitated by pervasive corruption and a lack of both expertise and checks and balances in the constitution that was amended in December 2004 (taking effect on 1 January 2006). The latter essentially established a parliamentary-presidential system, reallocating power and competencies between president, government and parliament.

In February 2010, Viktor Yanukovich won the presidential election with a narrow margin and Yulia Tymoshenko became leader of the opposition. The following years revealed his true intention, namely to concentrate all the power in his hands: Yanukovich repealed the amendments to the constitution passed in 2004 and returned Ukraine to a semi-presidential system. Human rights as well as freedom of expression and assembly deteriorated. The opposition, harassed by a subservient judiciary, proved weak and unable to withstand these developments.

When President Yanukovich declined to sign the Association Agreement with the EU in November 2013, unexpected mass protests broke out that ended at the end of February 2014 when Yanukovich fled the country. The mass protests ended the authoritarian rule and opened up a window of opportunities to overhaul the system of governance.

Until 2000, Ukraine's economy was in transformation recession. The first ten years of independence were marked by hyperinflation, high unemployment and falling standards of living.

Ukrainian authorities opted for gradual reforms (as opposed to Poland's shock therapy), resulting in dragged-out reform processes without clear-cut policy successes.

Amid sluggish reforms, influential industrial-economic groups and oligarchs emerged and a patron-client relationship between the president and these groups developed. This was reinforced by non-transparent large-scale privatization. Due to flawed procedures and favoritism, many large enterprises were sold far below market value and ended up in the hands of these groups.

Nevertheless, between 2000 and 2008, Ukraine enjoyed a period of economic growth fueled by favorable external market conditions. Real GDP grew at about 7% on average. By 2005, the private sector's share of GDP reached 65%. Poverty was reduced and disposable incomes increased.

The financial sector crisis that hit Ukraine 2008 revealed all deficiencies of incomplete reforms, which were partly forgotten amid the economic growth of the preceding years. Although the economic situation stabilized in 2010, the country did not return to a path of stable growth. Ukraine continued to suffer from non-transparent clientelistic politics and structural imbalances. Yanukovich's economic policy and corruption exacerbated the situation even more, almost bringing the country to default.

Until 2014, when the Association Agreement with the EU was finally signed and ratified, Ukraine maintained a balanced foreign policy between Russia and the West. After the Orange Revolution, the Ukrainian government drew closer to NATO and the European Union, while relations with Russia deteriorated. However, Ukraine's hopes for EU membership candidacy and the NATO Membership Action Plan did not materialize. Ukraine became a part of the European Neighborhood Policy and later the Eastern Partnership Initiative.

Meanwhile, relations with Russia became quite difficult. There were repeated trade conflicts as well as conflicts over gas deliveries, transit and payments. Moreover, Russia attempted to block the signature of the Association Agreement between Ukraine and the EU and make Ukraine join its Eurasian Economic Union. To no avail: Russia's military aggression and the annexation of Crimea ended the balancing act. The post-Euromaidan authorities embarked on a clear pro-European course, backed by an overwhelming support for the EU and NATO in Ukraine's public opinion.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

## Transformation Status

### I. Political Transformation

#### 1 | Stateness

Question

Score

The state does not hold a monopoly on the use of force throughout the territory of Ukraine. The state's monopoly on force was already partially disrupted during the last and most violent stage of the Euromaidan protests in February 2014, when protesters in some cities of Ukraine took hold of several weapon storage facilities. However, it should be noted that the state abused its monopoly on force during the Euromaidan protests. Protesters were brutally beaten on numerous occasions and later on shot by snipers - an obvious violation of the law on the part of the law-enforcement authorities.

Monopoly on the use of force

5

Later, in March 2014, Crimea was occupied and annexed by Russia. This was followed by forceful occupation of public buildings and the taking of control of entire districts of the Luhansk and Donetsk regions of Ukraine by pro-Russian militants and with clandestine, yet obvious, full-scale military support from Russia.

Another phenomenon that undermines the state monopoly on force is the emergence of a number of volunteer battalions as a response to the separatists' activities and the weakness of Ukrainian army during the initial stage of the war. Some 80 different volunteer battalions are engaged in military operations in Donbass. Although the battalions are subordinated to the central command of the so-called Anti-Terrorist Operation led by the Ukrainian security service, they are not part of the army command chain and are equipped mostly through the support of civilian voluntary initiatives. Soldiers returning from the front might present a challenge if they are not offered re-integration opportunities.

The Ukrainian nation-state is accepted by all relevant actors and groups in Ukraine, apart from Crimea and the territories in the east of the country under the control of pro-Russian insurgents.

State identity  
8

Identification has been growing in recent years. All citizens enjoy the same civil rights. In 1991, every person residing in Ukraine was entitled to Ukrainian citizenship, regardless of nationality. Ukraine thus emerged as a civic nation, and the nation-state's legitimacy is accepted by all relevant groups. Ukraine does not recognize dual citizenship, but the law on citizenship does not punish it. As a result, there are cases of acquisition of Russian, Romanian and Hungarian citizenship by Ukrainians, especially in western Ukraine and Crimea. Many (elderly) members of the Roma minority do not have Ukrainian passports.

Identification with the Ukrainian state reached its peak after the Euromaidan protests. Putin's belief that Russian-speaking Ukrainians are loyal to the Russian state proved highly questionable. The 2001 census (the most recent one) had already revealed that 77.8% of people self-identified as Ukrainian, while 17.3% self-identified as Russian. At the same time, 67.5% identified Ukrainian as their mother tongue, while 29.6% identified Russian as their mother tongue. Opinion polls conducted after the Euromaidan showed that identification with the Ukrainian state as compared to other identifications (for instance, local or regional) grew significantly. The number of people who identify themselves primarily as citizens of Ukraine grew from 54% in December 2013 to 73% in December 2014.

Church and state are separated and the political process is secularized. The heterogeneous religious landscape, combined with the secular Soviet past, prevents the impact of religious dogmas on state policy. There are five major churches: the Ukrainian Orthodox Church (Moscow Patriarchate), the Ukrainian Orthodox Church (Kiev Patriarchate), the Ukrainian Autocephalous Orthodox Church, and two Catholic churches (Greek and Roman Catholic). None of them function as a state church. In addition, there are Jewish and Muslim communities and a growing number of Protestant as well as Evangelical groups.

No interference of  
religious dogmas  
9

The Ukrainian Orthodox Church (Moscow Patriarchate) has the largest number of parishes, while the Ukrainian Orthodox Church (Kiev Patriarchate) has the largest number of adherents. The Ukrainian Greek-Catholic Church is the third-largest and dominates in the west of Ukraine. Other churches have respective shares of less than 3%.

There are no conflicts between the churches and the state. During election campaigns, political parties and individual politicians sometimes use the support of certain religious organizations. The church played a remarkable role during the Euromaidan. It openly supported the protesters (with the exception of the Ukrainian Orthodox Church of the Moscow Patriarchate), and representatives of all churches appeared regularly on stage at the Maidan (often together), trying to encourage the protesters and condemning violence.

Public administration functions on all administrative levels (with the exception of Crimea and the separatist-controlled areas of Donbass), albeit with varying degrees of effectiveness and state capture by economic actors. The low degree of decentralization also hampers more effective administration.

Basic  
administration  
7

With regard to public infrastructure, 98% of the population has access to running water and 95% has adequate access to improved sanitation facilities. The infrastructure has not yet been reconstructed in some parts of the Donetsk and Luhansk regions that were regained by Ukraine from insurgents.

## 2 | Political Participation

The distribution of political offices takes place through general elections, which are conducted regularly, where universal suffrage with secret ballot is ensured and several parties with different platforms are able to run. However, electoral legislation has remained highly unstable and undergone changes every time before elections.

Free and fair  
elections  
8

During the Yanukovich presidency, the quality of the electoral process significantly deteriorated. This was reversed after the Euromaidan. Both elections - for president in May 2014 and for parliament in October 2014 - were recognized as free and fair by domestic and international observers. There were irregularities in a few single-mandate constituencies, such as members of the electoral committees being threatened or replaced, lawsuits and conflicts on the day of voting, but these did not affect the overall outcome of voting.

Elections scheduled for October 2014 did not take place in the 10 single-mandate constituencies in Crimea and in 17 of 32 single-mandate constituencies in the Donetsk and Luhansk regions that were controlled by pro-Russian militia. This means that these seats will remain vacant in the Verkhovna Rada until it is possible to carry out elections in the respective constituencies.

Elected rulers have the power to govern. The ruling coalition has the constitutional majority in the parliament and is capable of passing decisions. It also has a professional government. Moreover, the president enjoys relatively high support in society and has the resources to promote certain decisions or block those that are harmful for the reform process. The president and the prime minister have so far been able to work together, although their relationship is not free of conflict. The above indicates that formally the authorities have the power and resources need to govern.

Effective power to  
govern  
6

However, politics is not independent of big business. The latter has acquired a firm grip on the economy and decision-making over the years of Ukraine's independence. On the positive side, big business does not act uniformly: there are different oligarchs who pursue different agendas and compete with each other. This fact alone accounts for pluralism in politics and informational space. Among other veto-players are

powerful actors at the regional and local levels who can undermine implementation. This is the case in Donbass, where Yanukovich's clientele was and still is influential. This partially accounts for negative developments in the region.

Freedoms of association and assembly are guaranteed in the constitution. However, during the Presidency of Viktor Yanukovich in 2010-2014, the practice of banning protests by court decision became widespread. Moreover, the government dealt violently with the peaceful Euromaidan protests, as it had done with smaller protests before. This led to the radicalization of the protest movement. In January 2014, laws were passed that made the very act of protest illegal and NGOs were labeled "foreign agents." Over 80 protesters lost their lives in the final days of the Euromaidan, allegedly shot by snipers.

Association /  
assembly rights  
9

The Euromaidan revealed that the protest potential in society has become higher. A study based on the analysis of some 200 online Ukrainian media resources showed that at least 3,950 protest actions took place throughout Ukraine between 21 November 2013 and 23 February 2014. This is more than during the whole of 2013 up to 20 November (3,428) and more than the annual average for 2010-2012. Freedom of assembly has been widely respected since the protests ensured the transition of power.

Since the end of the Euromaidan, numerous peaceful gatherings have taken place throughout Ukraine either in support of territorial integrity of Ukraine or in support of separatist activities (the latter in smaller numbers). Peaceful gatherings organized by civil society activists near the public buildings to advocate certain laws and decisions have taken place on numerous occasions and civil society organizations have faced no restrictions in their activities.

The prohibition of censorship in Ukraine is guaranteed by the constitution, by the Law on Information, and by the Law on Television and Radio Broadcasting. During the Presidency of Viktor Yanukovich, freedom of expression was not respected: according to the Reporters Without Borders World Press Freedom Index, Ukraine's rank dropped from 89th in 2009 to 127th position in 2014 out of 175 countries across the world. Since the end of the Euromaidan, the practice of media censorship has been eliminated. Journalists who lost jobs during the presidency of Yanukovich due to changes in media ownership were able to return to work in new media outlets.

Freedom of  
expression  
8

In addition, the Law on Public Broadcasting was adopted in April 2014. For public broadcasting to be fully operational, a number of amendments to this law still have to be passed. Other urgent reforms include transparency of media ownership and reform of state-owned media.

Ukrainian citizens have access to a variety and plurality of both print and electronic media, at least at the national level. The number of Internet users grew rapidly, to

over 50% in 2013 and the pace of growth is 16% per year. At the local level, many media outlets continue to be owned by the authorities or by oligarchs.

There have been several attempts to pass laws to restrict “Russian propaganda” and leading state officials have demanded action against popular TV stations for broadcasting “Russian propaganda.” The display and sale of Russian films produced since 2014 and of films presenting Russian security and military services in a positive light was banned by law in February 2015.

### 3 | Rule of Law

The Ukrainian Constitution provides for the separation of powers. During the presidency of Viktor Yanukovich, this separation was blurred, as he amended the constitution by court decision to increase his powers, and managed to put almost all state institutions, including the judiciary, under his control.

Separation of  
powers  
7

On the final day of the Euromaidan, the constitution was amended again, returning it to the version that was in place after the Orange Revolution. It provides for a semi-presidential system and strengthens the parliament and the government considerably. Although the ruling coalition has an overwhelming majority, parliament has demonstrated that it is able to put a check on the government.

The political independence of the judiciary and law-enforcement has not yet been fully achieved, largely due to the highly volatile political situation in the country. However, there are several initiatives under way to rectify these unpleasant shortcomings.

After judicial reform in 2010, the entire judicial system became dependent on the administration of President Yanukovich. Judges were forced to censor their opinions not only where there were instructions to do so, but also in the absence of these instructions.

Independent  
judiciary  
6

Following the transition of power after the Euromaidan, the judges had once again to adjust to the new political reality. The law “On Restoring the Trust in the Judicial System of Ukraine,” adopted in April 2014, authorizes judges in each court to elect the court’s president (who was previously appointed in a centralized manner). However, in the majority of the courts, control has been maintained by the very same people as previously. This problem is supposed to be addressed as a part of the lustration process, which still has to meet the requirements of the Venice Commission of the Council of Europe.

A system that would address the problem of appointment and promotion of judges is still absent. The law “On the Judiciary and Status of Judges” does not define any objective criteria, except for experience as a judge. Moreover, there are no

recommended provisions on competition for vacant positions. Decisions relating to the transfers of judges (both horizontal and vertical) are non-transparent and do not follow any objective criteria as the law does not specify any such criteria, nor does it require a competitive procedure for professional promotion.

Political corruption is still widespread in Ukraine, but thus far, there have been barely any cases where anyone has been brought to justice. A number of anti-corruption initiatives, among them the establishment of the Anti-Corruption Bureau, were adopted after the Euromaidan, but these are still awaiting implementation. The head of the National Anti-Corruption Committee, a famous anti-corruption activist, resigned in August 2014, claiming that “there is no political will in Ukraine to carry out a hard-edged, large-scale war against corruption.”

Prosecution of  
office abuse  
5

The process of lustration, launched with the adoption of the respective law in September 2014, includes conflict of interest as a criterion that prohibits taking public office, but the law is still subject to amendment.

Civil rights in Ukraine were severely violated during Yanukovich’s presidency, particularly during the Euromaidan, where many activists were detained, tortured, kidnapped from hospitals and treated with violence. Moreover, the prosecutor’s office, the Interior Ministry, the state security service and tax authorities were used as instruments of repression against the opposition, civic movements and business enterprises.

Civil rights  
7

The situation has considerably improved following the transition of power in February 2014. The government reduced the level of interference in tax and other controlling authorities in the functioning of business. In addition, the powers of the prosecutor’s office for general supervision have been revoked. These powers allowed for the carrying out of inspections of any business, thus significantly increasing prosecutors’ punitive actions and the risk of corruption.

However, it is still difficult for an individual to protect his/her right in the courts of general jurisdiction if those are violated by an unconstitutional act of the president or the government, as individuals do not have the right to apply to the Constitutional Court directly in these instances.

Freedom of movement and freedom of religion are, by and large, ensured and there is no noteworthy ethnic discrimination. Alleged discrimination of Russian speakers in the eastern and southern parts of the country are trumped-up propaganda stories.

In May 2014, amendments to the law “On Prevention and Countering Discrimination” were adopted (the initial law was adopted in 2012). These amendments broaden the list of grounds for discrimination and include, inter alia,

such grounds as age, skin color, physical condition (disabilities), family status, and sexual orientation.

However, there were cases when law enforcement agencies were not able to protect individuals associated with Yanukovich's regime, who became victims of "people's lustration" (were thrown into trash bins) or of black people and members of sexual minorities who were assaulted in public.

#### 4 | Stability of Democratic Institutions

Since the end of Euromaidan protests, major democratic institutions have been re-established. Ukraine returned to the constitution that ensures the power-sharing between the president and the parliament/cabinet. Early presidential and parliamentary elections took place, both having been free and fair and with a remarkably high turnout.

However, the effectiveness of these institutions is partially impaired as a result of their capture during Yanukovich's presidency. The judiciary, the civil service, the Office of the General Prosecutor and other institutions are still dominated by people appointed by Yanukovich and who were loyal to him. To solve this problem, a lustration law was adopted in September 2014. The law envisages that civil servants, judges, employees of law-enforcement authorities and other public institutions will be assessed according to several criteria (activities during Soviet times, activities during the presidency of Yanukovich and conflicts of interest); should it be established that they were involved in such activities, they will be banned from taking public office for 10 years. The law was criticized by human rights groups in Ukraine and by the Venice Commission of the Council of Europe. As the result, a working group on lustration was created that will propose amendments to the above-mentioned legislation.

Apart from these legacies, a number of other factors still hamper the functioning of democratic institutions. These include poor delineation of powers between the president and the prime minister, poor delineation of powers between the representatives of the executive vertical and elected authorities at the local level, and inefficiency in the civil service, law-enforcement authorities and judiciary. A number of reform initiatives to address these issues have been launched or are still on the agenda.

Performance of  
democratic  
institutions  
6

All influential political actors formally accept democratic institutions – at least in rhetoric and in political programs. No political force claims that democracy is alien to Ukraine or that it has been imposed from outside.

Commitment to democratic institutions

8

However, in practice there is a temptation to misuse and abuse political power and therefore undermine democratic principles. Political culture in Ukraine is not mature enough and democratic institutions are very fragile. Many political actors seem unaware of some of the basic ideas of a democratic system, such as respect for opponents' views.

Moreover, some democratic institutions are not accepted as legitimate on the basis of accusations that they are still controlled by anti-democratic forces related to former president Yanukovich. This also applies to parts of the judiciary.

Associations, civic organizations, and the military work within democratic norms, while some interest groups, such as oligarchs, still prefer informal networks to promote their interests.

## 5 | Political and Social Integration

The party system in Ukraine is very unstable and volatile. There are numerous political projects, rather than parties, that appear and disappear depending on the context. They have no clear differences in programs and continue to be primarily political vehicles for individual leading politicians, rather than aggregating and representing societal interests. On the whole, the battle lines between parties are blurred and change frequently, driven by power interests rather than ideology or party programs.

Party system

3

Before the early parliamentary elections in October 2014, the party system in Ukraine underwent another significant reshuffle. Most political parties that passed the 5% threshold are newly registered, although with the same old politicians. This applies to the “presidential” political party, the Petro Poroshenko Block (the largest faction with 147 seats); the People’s Front (the second-largest faction with 83 seats) of Arseniy Yatseniuk (the current prime minister); and the Oppositional Block (the third-largest faction with 40 seats) composed of former Yanukovich allies and representatives of the Party of Regions. The latter played an important role in Ukraine’s political life over the past 10 years, but disintegrated after the former president Viktor Yanukovich fled to Russia.

The Self-Help faction of the Mayor of L’viv Andriy Sadovyi (32 seats) and the Radical Party faction of Oleh Lyashko (22 seats) are relatively new political actors without experience in public posts. The first party includes a lot of young professionals and representatives of civil society, while the second is a populist party.

The smallest faction, with 19 seats, is Yulia Tymoshenko's Fatherland, which is the only party with a long tradition.

The fragmentation of the party system is low. Only a small number of parties get into parliament, although many more run elections (52 political parties ran in October 2014, but only 6 succeeded). In addition, the parties representing the pro-Maidan electorate (all of the above-mentioned parties apart from the Oppositional Block), were able to form a coalition and have the constitutional majority in the parliament. The non-Maidan electorate, which is concentrated in the south and east of Ukraine, also received representation by the Oppositional Block.

Although several new political parties that grew out of civil society, such as Democratic Alliance or The Power of People, represent a new quality of political parties, they have no chance to become visible and successful political actors due to the current rules of the game. Lack of state funding for political parties and lack of party funding transparency provide advantages to those parties or political projects represented by well-known politicians. These parties and projects are backed by substantial private funding coming from oligarchs.

At the national level, the formal channels for communicating societal or group interests are not well defined. The network of interest groups is relatively close-knit, but their possibilities for influence are very unequal.

Civil society has managed to increase its presence in public discourse and policy-making by forming platforms and coalitions. Such coalitions include New Citizen, which focuses on advocating better access to information; Stop Censorship – a movement of over 130 journalists, civil society activists, and NGOs aimed at reporting any violations of the freedom of media and at advocating media freedom; and Chesno – a network of more than 150 organizations, aimed at alerting Ukrainian society of potential members of parliament with a record of corruption and other problems. After the Euromaidan, the so-called Reanimation Package of Reforms (RPR), with some 300 experts in various reform areas, was launched. Crucially, the RPR has a counterpart in the parliament – the Platform of Reforms, which is a group of 24 MPs from different parties. The Reforms Support Centre to the Cabinet of Ministers, which bridges the government and the RPR, was also created.

Financial-industrial groups or oligarchs are well represented in decision-making, although mostly through non-transparent channels. Such oligarchs as Rinat Akhmetov, Dmytro Firtash, Ihor Kolomoyskyi or Viktor Pinchuk, to mention a few, own popular media, finance political parties or influence the government through informal channels and thus ensure that their interests are represented in decision-making. According to a recent public opinion poll, 90.3% of Ukrainians think that oligarchs continue to be an “influential political and economic force in the country.”

Interest groups

6

Other societal interests are less well represented. Ethnic, nationalist and religious mobilization has not played a role in the constellation of interest groups in Ukraine. Despite relatively high formal membership in trade unions, these have played a marginal role in promoting issues important for employees, such as workplace safety or better social conditions. Consumers in Ukraine, although potentially the largest interest group, have not been sufficiently organized to influence policy. Business associations have started thinking about their interests in view of the Association Agreement with the EU and have begun representing these to the government. However, the influence of such groups has remained weak, not the least due to their low capacity to conduct impact assessments and articulate their interests.

The people of Ukraine generally endorse democratic norms, but with specific connotations. Surveys show that the quality of democracy is mainly assessed by the state's ability to deliver social welfare and keep the economy running. Moreover, given the significant deterioration of the economic situation and the war in Donbass, priorities related to survival prevail over democratic values. In December 2014, a representative survey conducted by the Democratic Initiatives Foundation revealed that people consider the top problems to be solved the normalization of the situation in Donbass and reaching peace (79%), improving the material situation and increasing salaries and pensions (48%), providing for economic growth (43%), fighting corruption (34%) and strengthening the national currency, fighting inflation and the growth of prices (29%). Other problems mentioned in the survey include the need to carry out constitutional reform (12.5%), providing for accountability of authorities (12.3%), decentralization and development of local self-governance (5.5%), reforming election legislation (1.8%), and fostering free media (1.3%).

According to the same opinion poll, attitudes towards the Euromaidan protests are mixed, even though the latter brought an end to the de facto authoritarian system and enabled free and fair elections and other political freedoms. Although 40.8% considered the Euromaidan (or the Revolution of Dignity) to be the top political event of 2014, only 31% consider this event to be a positive one, while 50.8% consider it to be a negative event. Most probably, for many people, the Euromaidan is regarded as a cause of the turbulent events Ukraine has been experiencing since then. Indeed, in December 2014, 57.7% thought that the developments in Ukraine are moving in a negative direction, while only 21.7% had a positive opinion of these developments. Moreover, the number of people who thought that the level of democracy, respect for political freedoms and human rights, and freedom of speech had deteriorated in 2014 outweighed the number of people who thought that the situation had improved.

Public trust in political institutions remains low, but higher than in 2013. The presidency of the Ukraine is the only political institution enjoying more public trust than mistrust (a big contrast compared to the presidency of Yanukovich) – 49.4% vs 44% respectively. The Ukrainian army also enjoys the trust of the population: 57.9% trust vs 33.4% mistrust. The level of mistrust exceeds the level of trust when it comes

Approval of  
democracy

6

to the parliament (31.2% trust vs 56.9% mistrust) and the government (35.8% trust vs 54.2% mistrust). The law-enforcement authorities and judiciary enjoy much higher levels of mistrust.

The growth of social capital in Ukraine has been remarkable, both during the Euromaidan protests and afterwards. Unlike the Orange Revolution, where the oppositional political parties took care of the infrastructure that supported the protests, the decisive role during the Euromaidan protests was played by civil society organizations, voluntary initiatives and ordinary people. From the very first day of the protests, civil society was quick to organize the necessary infrastructure to support the Euromaidan and to coordinate the donation of funding, food, clothes, medicines and voluntary involvement on behalf of ordinary people. When violence was exercised against the protesters, a number of initiatives emerged that compiled lists of people who were injured, missing or in detention, and a medical service and self-defense units were established. The following initiatives bear particular mention: AutoMaidan – a movement of car owners who developed a special form of protest by using their cars to provide protesters with help or even to protect the barricades from the police; Euromaidan SOS – an initiative that gathered information on people who needed help (missing, detained, injured, etc.) – after the protests it turned into an initiative helping people who fled from Crimea and the warzone in eastern Ukraine; an initiative of lawyers who offered free legal assistance; and the Civic Sector of Euromaidan – mostly young people representing NGOs, who not only volunteered at Maidan, but also provided their expertise to international organizations trying to influence developments in Ukraine, and produced regular updates in English about the developments in the country. According to a public opinion poll conducted by the Democratic Initiatives Foundation, the number of people who belonged to civic movements – most of which emerged specifically to meet various Maidan needs – more than doubled between December 2013 (6%) and February 2014 (14%). This took place despite the fact that the majority of protesters (70%) were not affiliated with any political parties, civil society organizations or movements.

After the Euromaidan, in the face of Russian aggression, people were eager to donate to the army and voluntary initiatives providing support to the army, voluntary battalions and the civilian population impacted by the war. According to the data of the largest Ukrainian bank, PryvatBank, which launched a special support program for the army, Ukrainians donated over 3.4 million Ukrainian hryvnia (UAH) (ca. € 150,000) to the army between June and September 2014. According to an opinion poll, 77.7% of Ukrainians supported the army and internally displaced persons between May and September 2014. Given this, it is not surprising that voluntary initiatives top another opinion poll asking about the level of trust in public and civic institutions in Ukraine: on a scale from 0 to 10, trust in volunteers reached 7.3 points, far above the level of trust in public authorities.

Social capital

7

The level of trust in NGOs has also increased, with the level of trust exceeding the level of mistrust for the first time: in December 2014, 43.6% trusted NGOs, while 34.8% mistrusted them. In total, there were more than 75,000 registered NGOs in Ukraine in 2014 (representing an increase of over 20,000 since 2008). However, some estimates claim that only about 10% of these are active.

## II. Economic Transformation

### 6 | Level of Socioeconomic Development

After a temporary improvement in 2013, poverty increased in Ukraine in 2014 amid political and economic crises and military aggression against the country.

According to Ukrstat, the state statistics service of Ukraine, relative poverty (measured as the share of the population with an equivalent total monthly income below the national poverty line – subsistence minimum) was 8.4% in 2013 compared to 9.1% in 2012 and 7.8% in 2011. However, poverty grew again in 2014 as real disposable income dropped and part of the population became refugees after the annexation of Crimea and occupation of Donbass. In addition, poverty grew in the occupied territories of Donbass. According to assessments by international organizations, over 630,000 people became internally displaced and 5 million people are still inside the zone of military action, many of them in need of humanitarian assistance.

Real disposable household income dropped by 19.2% year-on-year in the fourth quarter of 2014, marking the first year of negative growth for the first time since 2009.

Nevertheless, Ukraine is ranked 83rd out of 187 countries in the 2014 Human Development Index (HDI) and belongs to a group of countries with high human development. Ukraine's score is 0.734. The inequality-adjusted HDI score is 0.667, placing Ukraine 18 places higher than the standard HDI for 2014. The Gini coefficient for Ukraine is 25.6, a level of more developed countries.

Despite the officially declared non-discrimination principle, there are signs of gender inequality. Ukraine's rank in the Global Gender Gap Index was 56th out of 142 countries in 2014. Women have equal access to education, the social protection system and labor force participation, but are not fully included in political life and sometimes receive lower wages for equivalent positions.

There are no specific social barriers associated with religion, but social exclusion is registered for some ethnic minorities like the Roma, as well as for disabled people and people with HIV/AIDS.

Question  
Score

Socioeconomic  
barriers

5

| Economic indicators        |          | 2005    | 2010     | 2013     | 2014            |
|----------------------------|----------|---------|----------|----------|-----------------|
| GDP                        | \$ M     | 86141.5 | 136419.3 | 183310.1 | <b>131805.1</b> |
| GDP growth                 | %        | 2.7     | 4.2      | 0.0      | <b>-6.8</b>     |
| Inflation (CPI)            | %        | 13.6    | 9.4      | -0.3     | <b>12.2</b>     |
| Unemployment               | %        | 7.2     | 8.1      | 7.9      | -               |
| Foreign direct investment  | % of GDP | 9.1     | 4.7      | 2.5      | <b>0.6</b>      |
| Export growth              | %        | -11.2   | 4.5      | -8.1     | <b>-14.5</b>    |
| Import growth              | %        | 2.1     | 11.1     | -3.5     | <b>-22.1</b>    |
| Current account balance    | \$ M     | 2534.0  | -3016.0  | -16518.0 | <b>-5332.0</b>  |
| Public debt                | % of GDP | 17.1    | 40.6     | 40.7     | <b>71.2</b>     |
| External debt              | \$ M     | 33720.9 | 125172.8 | 147712.4 | -               |
| Total debt service         | \$ M     | 5713.3  | 27151.5  | 37833.4  | -               |
| Cash surplus or deficit    | % of GDP | -1.4    | -6.5     | -        | -               |
| Tax revenue                | % of GDP | 17.1    | 15.5     | -        | -               |
| Government consumption     | % of GDP | 18.6    | 20.3     | 18.2     | <b>18.6</b>     |
| Public expnd. on education | % of GDP | 6.1     | -        | -        | -               |
| Public expnd. on health    | % of GDP | 3.8     | 4.4      | 4.2      | -               |
| R&D expenditure            | % of GDP | 1.17    | 0.83     | -        | -               |
| Military expenditure       | % of GDP | 2.8     | 2.7      | 2.4      | <b>3.1</b>      |

Sources (as of October 2015): The World Bank, World Development Indicators 2015 | International Monetary Fund (IMF), World Economic Outlook, October 2015 | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database 2015.

## 7 | Organization of the Market and Competition

The essential elements of a market economy are in place in Ukraine. Most of the prices are formally liberalized. According to the EBRD, Ukraine's price liberalization score has been 4 (on a scale from 1 to 4+) since 1997. The government intervenes in price setting for selected products deemed socially important (some food products, medicines). In addition, utility, energy and telecommunication tariffs are regulated by special regulatory bodies. The Anti-Monopoly Committee of Ukraine is responsible for the prevention of unfair competition and abuse of market power.

Market-based  
competition

6

Market entry barriers are moderate. According to the Doing Business Report 2015, Ukraine is ranked 76th in the category of starting a business. The country fell 7 places compared to the previous report due to improvements registered in other countries, while the duration and costs of starting a business in Ukraine remained unchanged.

Market exit remains difficult. Ukraine is ranked 142nd out of 189 economies in the category of resolving insolvency. Both the time and the cost of the procedures are much higher than the regional average, while the recovery rate is low.

Ukraine has quite an open trade regime for goods and the majority of services. Ukraine is open to the inflow of foreign capital. Foreign companies registered with local authorities receive important guarantees:

- foreign investment cannot be nationalized or subject to requisition, except with force majeure events, and in these cases investors have the right for restitution of losses; and
- investors have the right to unimpeded repatriation of profits, dividends and investments after all due taxes are paid. In 2014, administrative capital controls were introduced to stabilize the foreign exchange market.

Ukraine's national currency – the hryvnia - is not fully convertible. Ukraine adopted the current account convertibility under the IMF's articles in 1997, but foreign investors still face currency control difficulties.

However, there are several important drawbacks. The size of the shadow economy significantly distorts the allocation of resources and undermines competition. According to the last publicly available estimates of the Ministry of Economic Development and Trade of Ukraine, the shadow economy represented 34% of GDP at the beginning of 2012. It grew in 2013-2014 amid political and economic turmoil.

Formally, rules are the same for all market participants, but de facto, the economy features the dominance of financial-industrial groups and state capture. The judicial system is weak and unable to effectively protect market participants.

The new government, appointed in 2014, promised to conduct comprehensive reforms to fight corruption, ensure the rule of law and market-based competition. In addition, the signing and ratification of the Association Agreements with the EU in 2014 creates an important anchor for market-based economic reforms in the country. However, most reforms are still being prepared and their impact will be seen in the years to come.

Competition laws are in place in Ukraine, but their enforcement remains rather weak.

There are several public bodies responsible for the prevention of unfair competition and facilitation of competitive practices. The key authority is the Anti-Monopoly Committee of Ukraine (AMC), established in 1994. Price setting in energy, utilities and telecommunication is regulated by respective national commissions, special regulatory bodies.

The responsibilities of the AMC include the prevention of unfair competition and abuse of market power, the control over concentration and collusion, the control over price setting in natural monopolies, and the protection of competition in public procurement.

The AMC is controlled by the president of Ukraine, and reports to the Verkhovna Rada. As with other public institutions, a public (advisory) council has exercised public control over AMC activities since 2005. The council is comprised of 38 members representing Ukraine's major industry associations and NGOs.

The AMC faces several, mainly institutional and legislative shortcomings, including lack of autonomy, investigative tools and transparency. The AMC has not made sufficient use of the imposition of harsh sanctions and fines to deter cartels or prevent abuse of market power. In addition, the actions of different state bodies have not been always synchronized and often counteract the AMC's efforts.

The Association Agreement between Ukraine and the EU signed in 2014 envisages a harmonization of Ukrainian legislation with EU norms in the sphere of competition. The implementation of these provisions is expected to introduce much higher standards of competition policy. However, it will take several years to see results.

Existing shortcomings result in poor scores of Ukraine's competition policy in international ratings. In particular, according to the EBRD Transition Report 2014, Ukraine's score in competition policy has remained at 2+ (on scale from 1 to 4+) since 1997.

Anti-monopoly  
policy

6

Ukraine's foreign trade is sufficiently liberal, although some exceptions exist.

The country has been a WTO member since 2008. It has also signed a number of FTAs, including bilateral FTAs with all CIS members, a CIS FTA, and a FTA with EFTA. In 2014, Ukraine signed the Association Agreement with the EU, envisaging the establishment of DCFTA (coming into effect as of 2016). The EU has granted Ukraine autonomous trade preferences since April 2014.

For imports of agricultural products, the average MFN applied tariff rate is 9.5%; for non-agricultural goods, it is 3.7%. The majority of import tariffs are ad valorem. Ukraine applies only one tariff quota, on raw cane sugar.

Export duties are applied to only few products, including some oil seeds, live animals, raw hides, natural gas, and scrap metal. The rates were significantly reduced after Ukraine joined the WTO.

Import and export licenses are required for a limited number of goods. The list of goods requiring licenses for foreign economic transactions is adopted annually by the Cabinet of Ministers.

Ukraine progressed in reforming technical barriers to trade. In 2014, Ukraine facilitated harmonization of its TBT and SPS-related regulations, aiming to take advantage of opportunities presented by autonomous trade preferences and the DCFTA with the EU. All key horizontal laws in these spheres were passed by the end of 2014.

Ukraine has a two-tier banking system with the National Bank of Ukraine (NBU) as a supervisory and regulating body and commercial banks that serve economic agents. Formally, the NBU is independent, but de facto, it remains sensitive to political will.

The banking system is oriented in principle on international standards, namely the implementation of Basel II and Basel III, but lacks supervision.

As of the end of 2014, there were 165 licensed banks in the country, including 51 banks with foreign capital. Foreign statutory capital in the banking system was 32.2% at the end of 2014 compared with a 41.9% peak at the beginning of 2012. The bank capital to assets ratio was 15.1% in 2013.

The stability of the banking sector significantly deteriorated again in 2014 after the temporary improvement registered in 2013. The adequacy of regulatory capital (H2) was 14%, the lowest level since the 2008-2009 financial crisis. Both returns on assets and equity were negative, and banks report considerable stocks of non-performing loans. The share of non-performing loans reached 14.6% in 2014 (12.9% in 2013).

Liberalization of  
foreign trade

8

Banking system

6

The stability of the banking system was further undermined by an outflow of deposits. National currency deposits fell by 14% and foreign currency deposits fell by 37% against the background of economic crisis, military conflict and low trust in banks.

The sharp depreciation of the hryvnia once again highlighted the problem of currency mismatch. The volume of national currency loans was almost equal to the volume of foreign currency loans against the background of fast capital outflows and shrinking exports.

The stock market has not recovered after the 2008-2009 financial crisis.

## 8 | Currency and Price Stability

In 2014, Ukraine witnessed sharp depreciation of its national currency and growing inflation. According to Ukrstat, the Consumer Price Index increased by 12.1% on average in 2014. Price growth accelerated over the year and peaked at 24.9% in December, the highest level for more than a decade. Prices increased for all categories of products, including the regulated prices for utilities.

In February 2014, the National Bank of Ukraine (NBU) formally introduced a flexible exchange rate against the background of declining international reserves, capital outflows, and political and economic instability. Nevertheless, the NBU continued to manage the UAH/USD exchange rate both through market intervention and administrative measures, including the mandatory sales of exports receipts (initially it was required to sell 50% of export receipts, then 100%, and then 75%).

Despite changes in the foreign exchange regime, the NBU did not manage to avoid a deficit in the balance of payments. According to the NBU, the consolidated balance of payments deficit reached \$13.3 billion in 2014, compared to a \$2 billion surplus in the previous year. The deficit was formed by both the trade deficit and outflow of capital, including \$2.7 billion of foreign cash withdrawn from banks.

As a result, international reserves dropped sharply to \$7.5 billion as of the end of 2014, compared to \$20.4 billion at the beginning of the year.

Ukraine resumed active cooperation with the IMF in spring 2014 under the Stand-By Arrangement. The introduction of inflation targeting was defined as one policy goal, but not in the short-term.

Formally, the NBU is independent. De facto independence is still contingent on both the commitment of NBU leadership and government pressure.

However, the drastic rise in inflation and the massive devaluation of the national currency is not caused by a worsening institutional framework, but rather by worsening economic and financial conditions.

Anti-inflation /  
forex policy  
6

In 2014, Ukraine faced a recession provoked by a combination of economic and political factors, including political instability, military conflict in Donbass, Russia's annexation of Crimea, high state indebtedness and stalled reforms amid high levels of corruption.

Macrostability  
5

As of the end of 2013, Ukraine's total state debt reached 40% of GDP, having more than doubled over the last seven years. In 2014, state indebtedness surged further, and the total state debt reached 70% of GDP by the end of the year against the sharp devaluation of the national currency and new borrowing needed to finance Ukraine's obligations, cover fiscal deficits and recapitalize state-owned companies.

The consolidated fiscal deficit (not including the recapitalization of banks and Naftogaz) was about 5% of GDP in 2014, and 4.4% in the previous year. It was financed by borrowing.

The current account (CA) deficit was about 4% of GDP in 2014, lower than in 2013 (8.7% of GDP) due to depreciation, lower energy imports (resulting from gas price conflicts between Naftogaz and Gazprom) and the overall fast decline of imports given the reducing purchasing power of households and lower level of investment. However, the CA deficit was coupled with capital outflows.

Ukraine resumed active cooperation with the IMF after the change in political leadership. In April 2014, the IMF approved a two-year Stand-By Arrangement amounting to SDR 11 billion. As of the end of 2014, Ukraine received two disbursements of SDR 3 billion in total. Some urgent steps at fiscal consolidation, an increase in gas and heating prices, the approval of a new public procurement law, and stress tests for the largest banks were set as preconditions of the Stand-By Arrangement. Further fiscal consolidation and an increase in the efficiency of fiscal expenditure, a switch to inflation targeting, an active anti-corruption policy, energy sector reforms and an improvement in the business climate were earmarked as key reforms areas.

However, the speed of reforms in Ukraine has been lower than expected, partly due to military conflict and election campaigns. Meanwhile, the macroeconomic situation has continued to deteriorate. The new government, established after the October parliamentary elections, announced its commitment to conducting deep structural reforms in the country. Their success remains to be seen.

## 9 | Private Property

The Constitution of Ukraine as well as the Civil Code and Commercial Code guarantee the right to private property, including nonagricultural private land.

Property rights  
7

However, de facto property ownership is weakly protected because the court system is inefficient, corruption is extensive, and the judiciary is strongly influenced by other branches of government.

In 2014, the new president, parliament and government announced a set of reforms aimed at considerably improving the situation in this sphere, including judiciary reform, and strong anti-corruption measures. In mid-2014, a set of anti-corruption laws were passed. Although some improvements have been observed, these reforms are still in progress and their main impact is expected to be seen in the coming years.

Ukraine significantly improved its standing in the category of registering property in the Doing Business Report 2015 (which assessed the situation in mid-2014). The country is ranked 59th out of 189 economies, gaining 29 places as compared to the previous year and even more if older rankings are used. The improvement is due to the sharp reduction in the time taken to register properties.

At the same time, the World Economic Forum placed Ukraine at 135th out of 144 for property rights (no change in rank), and reduced its placing to 129th with respect to intellectual rights protection in the report for 2014-2015.

Private enterprises dominate Ukraine's economy by number, but account for a much lesser share of output. According to the EBRD, the private sector accounted for 60% of GDP in 2010.

Private enterprise  
7

The SME sector is large and expected to become one of the future economic growth drivers. According to official information, SMEs and private individuals/entrepreneurs accounted for over 99% of Ukraine's private sector enterprises, 76% of jobs and 60% of total sales in 2013. These figures have been gradually growing. According to the World Bank's Doing Business indicators, starting a business in Ukraine is not overly complicated, taking 21 days and including 6 separate administrative procedures.

In 2013-2014, the privatization process stopped. The parliament approved a state budget for 2015 with large privatization receipts target, but its implementation is conditional upon macroeconomic stabilization, an improvement in the business climate and a cessation of conflict on Donbass.

## 10 | Welfare Regime

Social safety nets are developed in the country and consist of two main components: services and money transfers. The system suffers from important shortcomings that undermine its efficiency, burden the budget, and impede equality. Many categories of aid and benefits are provided to a wide range of citizens, so that the total financial obligations exceed the country's means. Amid a difficult fiscal situation, social protection expenditure continued to grow and reached 27% of total central fiscal expenditure in 2014 (8.6% of GDP) in comparison with 2012, where this figure was 22% of fiscal expenditure or 7.8% of GDP. This figure also includes only part of pension spending, namely the spending covered by the state budget. Total pension expenditure amounts to 16% of GDP.

Social transfers and privileges are still poorly targeted. People receive benefits not because of their individual needs but because they belong to a defined social group. As a result, richer households receive considerably more privileges and benefits than poorer ones, while not all poor households are able to enjoy their privilege entitlement.

The pension system de facto consists of two pillars: the solidarity system (first pillar) and a non-state pension provision system based on voluntary participation (second pillar), although the development of the latter is limited by the weak stock market, low incomes and mistrust in financial institutions. The pension reform launched in 2003 has not been completed, as the second pillar - compulsory individually funded pension insurance - has not been introduced.

Pension payments have been growing slowly in hryvnia terms, but depreciation has considerably undermined the purchasing power of pensioners. In 2014, the average monthly pension was UAH 1,526 (less than \$100) and the minimum was UAH 1,218 (less than \$76).

The pension fund operates with a deficit, endangering the system and hampering reforms. Since 2011, the pension age has been gradually increasing both for men and women to reduce financial pressure on the pension fund. The pension age is set to increase from 55 to 60 for women, and from 60 to 62 for men. Life expectancy at birth in Ukraine is 70.9; higher for women and lower for men. Changes in the pension age have somewhat improved the financial stability of the pension fund but not to a degree sufficient to balance the fund's budget.

At the end of 2014, the parliament passed a law amending the administration of the social protection system to reduce spending and eliminate inappropriate functions of the social security funds.

Social safety nets  
6

Public expenditure on health was about 4.0% of GDP in 2013-2014. According to the constitution, health care is to be provided universally, efficiently and free of charge. However, in practice, Ukraine's health care system does not provide universal access to quality health care, spending patterns are inefficient, and informal payments are common. Health care reform is ongoing, but progress is limited.

Military conflict in Donbass further worsened social protection. People living in occupied territories do not have access to public social payments, and provision of other social services is at least partly disrupted. Internal migration (refugees) has put additional pressure on already stretched social safety nets.

Ukraine has established a legal framework for protection against discrimination, both in the constitution and in specific laws. The Law on Principles of Prevention and Countering Discrimination in Ukraine was passed in September 2012. The country has also joined international anti-discrimination conventions. However, the implementation of legal provisions against discrimination remains insufficient, resulting in inequality and social exclusion faced by some social groups.

Gender inequality is moderate. According to the Human Development Report 2014, the gender inequality index for Ukraine was 0.326 in 2013, an improvement on the 2010 score of 0.351. According to the Global Gender Gap Report 2014, Ukraine is ranked 56th out of 142 with a score of 0.706 (0 - inequality, 1 - equality). Women have full access to education and employment, but receive lower wages for equivalent positions and are much less represented in the political life of the country.

Disabled people and people with HIV/AIDS have unequal access to participation in society, including access to education and employment. People with disabilities remain excluded frequently due to the deficiency of both urban and rural infrastructure; namely the lack of adaptation of buildings, roads, transport etc. The exclusion of people with HIV/AIDS is largely due to the stigma associated with HIV status and population prejudices.

Social exclusion is registered for Roma, who are largely excluded from education, the labor market and social services.

The annexation of Crimea by the Russian Federation in March 2014 significantly worsened the protection of rights of Tatars due to discrimination by the Russian authorities.

Equal opportunity

7

## 11 | Economic Performance

Ukraine's macroeconomic parameters significantly worsened in 2013-2014. According to state statistics service of Ukraine (Ukrstat), in 2013, real GDP remained at the level of the previous year. In 2014, the economic situation further deteriorated, with the annual decline in real GDP estimated at 6.8%.

Output strength  
2

The reduction in real GDP was driven by a drop in final household consumption and in capital accumulation. Both exports and imports of goods and services dropped in real terms in 2014, but the speed of the reduction in imports was higher, allowing for positive contribution of net exports into real GDP.

The deterioration of the economic situation in the country was due to a number of factors, including:

- high political instability (the revolutionary events in November 2013-February 2014, early presidential and parliamentary elections);
- the annexation of Crimea and the military conflict in Donbass, resulting in loss of territory, broken production linkages, decreased access to energy and other raw materials, refugees and accelerated internal migration, mobilization etc.; and
- the debt and banking system crises.

On the production side, all major sectors of the economy demonstrated negative growth except for agriculture. In particular, industrial output dropped by 10.7% year-on-year in 2014 following a 4.3% year-on-year reduction in 2013 and 0.5% year-on-year decline in 2012. The reduction could be seen across almost all industries, excluding food and textiles. Construction fell by 21.7% year-on-year in 2014.

The growing agricultural sector partially counterbalanced the negative trends in other sectors. In 2014, agricultural output increased by 2.8% year-on-year.

The current account (CA) deficit narrowed in 2014 after the peak of the previous year. According to the NBU, the CA deficit was at \$16.5 billion or 8.7% of GDP in 2013, while in 2014, it was at \$5.3 billion or about 4.0% of GDP.

With net capital outflows, the balance of payments deficit reached \$13.3 billion or about 10% of GDP in 2014. Ukraine's international reserves thus dropped to less than 1.5 months of imports by the end of the year.

Unemployment increased amid the economic crisis and military conflict. In mid-2014, unemployment (ILO methodology) was estimated at 8.9% of the economically active population aged 15-70.

Consumer price inflation accelerated against the background of devaluation and stagnation of economic activity. The average consumer price inflation was 12.1% in 2014 as compared with -0.3% in 2013. The budget situation remains very difficult. The consolidated public deficit (not including the recapitalization of banks and Naftogaz) is estimated at 4% of GDP in 2014. Including the recapitalization of Naftogaz would boost this figure to about 10% of GDP.

In summary, the economy of Ukraine has entered a recession phase without having fully recovered from the 2008-2009 crisis.

## 12 | Sustainability

Formally, environmental issues are on Ukraine's policy agenda. In 2010, the Main Principles of the State Ecological Policy of Ukraine until 2020 were passed by parliament, and in 2011 the National Action Plan for Environmental Protection in 2011-2015 was adopted by the Cabinet of Ministers.

Environmental  
policy  
4

The Ministry of Ecology and Natural Resources of Ukraine analyzed the implementation of above-mentioned documents. According to the report, the progress of achieving of 1 out of 9 goals of the strategy was assessed as sufficient. This goal envisaged improvement of regional ecological policy. There was almost no progress in goals related to human health and environmentally friendly production.

In 2014, Ukraine was ranked 95th out of 178 countries in the Environmental Performance Index (EPI). Its score was 49.01, which represents a +5.44% ten-year trend. The still-low ranking of Ukraine is explained by problems in the preservation of biodiversity, the high carbon intensity of the economy and inadequate pesticide regulation.

Renewable energy has been gradually developing, partly thanks to green tariff regulation, but its share is still very low.

Energy saving technologies are making their way into Ukraine's life. This trend seems to be accelerating amid disruptions to energy supply from Russia and expected energy shortages.

There is an established system of state and private education and training in Ukraine. Primary and secondary education is provided for everybody, including citizens, foreigners and stateless persons.

Education policy /  
R&D  
6

The net enrollment rates are 97.9% for primary education, 97.8% for secondary education and 79.7% for tertiary education. The adult literacy rate remains high at 99.7% for ages 15 and older.

The expected years of schooling have increased and reached 15.1 years according to the Human Development Report 2014. Women tend to stay in educational institutions longer - 15.3 years as compared to 14.9 years of schooling for men.

According to the World Competitiveness Report 2014-2015, Ukraine is ranked 72nd out of 144 in the quality of the educational system, with a higher quality for math and science education (30th out of 144). The quality of primary education is also assessed as high (40th out of 144).

However, the quality of education varies greatly. Vocational and higher education suffer from a mismatch between labor market demand and the knowledge and skills provided by educational institutions.

In 2014, a new law on higher education was passed in the country, envisaging greater independence of universities and, as expected, stimulating the harmonization of Ukrainian higher education with the best international educational practices. Nevertheless, the impact of the law on the quality of higher education and, more importantly, on innovation, remains to be seen.

So far, the reasonable quality of education has not translated into innovation and thus has provided only a limited boost for the economic development of the country.

Insufficient protection of property rights and low expenditure on R&D hamper innovation in Ukraine. Financing of R&D as a share of GDP represents less than 1% of GDP. According to the state statistics service of Ukraine, the share of value added produced by the R&D sector was 0.8% of gross value added in 2012.

According to the World Competitiveness Report 2014-2015, Ukraine is ranked 113th out of 144 in terms of the availability of latest technologies, and firm-level technological absorption is also low (100th out of 144).

# Transformation Management

## I. Level of Difficulty

Ukraine faces several long-term structural constraints.

It is undergoing severe a demographic crisis, characterized by an aging and shrinking population. According to Ukrstat, the average life expectancy in 2014 was 66.3 years for men and 76.2 years for women. At 1.5 children per woman (2014), the country's fertility rate is insufficient to ensure the natural recovery of the population. This creates future economic and social problems.

At the same time, Ukraine is a country of labor emigration. Several million Ukrainians work (temporarily) abroad, mainly in the European Union and Russia. So far, policies and institutions have been ill-equipped to deal with the consequences of this development, which include higher expenditure for healthcare, care for the elderly, pensions, and a shrinking labor force.

The country's energy dependent and energy inefficient economy poses an additional structural constraint. Ukraine depends on Russia as a supplier of gas and oil, also because pipelines to Ukraine from Central Asia run through Russian territory. In June 2014, Russia cut off the gas supply and renewed it only at the end of 2014. The reverse supply of gas from the EU and some energy saving measures helped Ukraine to cope with the problem, but the measures introduced thus far are insufficient to solve the problem.

A new structural constraint arose in 2014. The annexation of Crimea and military intervention in Donbass resulted in a number of important problems for Ukraine: loss of control over about 3% of its territory (excluding Crimea), including losing access to mineral resources and mines (the latter responsible for electricity shortages); over 600,000 internally displaced persons, putting additional pressure on social safety nets; and broken production links. Moreover, Ukraine does not control a part of its border with Russia, through which support to pro-Russian fighters is supplied regularly. This means that military operations in Donbass will continue, creating an unprecedented level of expenses for the army, which in turn places constraints on a budget already exhausted by the economic crisis.

Structural  
constraints

8

Civil society traditions date back to pre-Soviet times. During the Soviet era, civil society was suppressed and controlled by the party state. Some major human rights organizations, such as the Ukrainian Helsinki Human Rights Union or the Kharkiv Human Rights Protection Group, have their roots in the Soviet human rights movement. The same applies to some charitable foundations.

Civil society traditions

4

In recent years, popular acceptance of and involvement in civil society has improved and, in December 2014, the level of trust in civil society exceeded the level of mistrust for the first time. Due to the Euromaidan and its aftermath, more people have shown a willingness to protest and to become volunteers.

Presently, only about 10% of officially registered Ukrainian NGOs work on a steady basis. Many of them depend on support from outside agencies. Although the legal environment for civil society improved in 2012 and 2013, it is still unclear to what extent NGOs can take advantage of it. However, the self-perception of civil society has significantly changed in recent years, especially after the Euromaidan protests. Civil society has become aware of its role in the reform process and has improved its advocacy activities through joining forces in networks and NGO coalitions, and exercising increased pressure on public authorities.

In general, there are some differences in the history and current formation of civil society across Ukraine's various regions, with the western regions being more exposed to international contacts and experience, and having demonstrated more involvement in protests. Moreover, there is a clear historical divide between urban centers and the countryside, with the latter having less-developed NGO networks.

Even though Ukraine is an ethnically, linguistically and religiously diverse country, conflicts of ethnic, linguistic or religious origin remain insignificant. None of Ukraine's five major churches constitutes a state church. Ukraine has liberal laws regarding religion, which also guarantee freedom of religious practice. Ukrainian, Russian and other languages are freely spoken in Ukraine. The pretext for Russian intervention in Ukraine – the alleged violations of the rights of the Russian-speaking population, had nothing to do with reality: Ukrainian media space is dominated by Russian-language products and Russian is spoken freely. Moreover, the protesters at the Euromaidan represented different ethnic communities, while several top politicians in Ukraine, including in the government, are of non-Ukrainian ethnicity.

Conflict intensity

9

The conflict in Donbass was not provoked by social, ethnic or religious cleavages, but by the desire of Russian insurgents, local fringe politicians and criminal elements, closely associated with the former president Yanukovich and his Party of Regions, to stage the "Crimean scenario." In addition, the Oppositional Block party created right before the parliamentary elections in October 2014 received 40 seats among 422 MPs and therefore has a say in policy-making. This party includes many representatives of the former Party of Regions and claims to represent the "non-

Maidan” spectrum of society. At the same time two radical right wing parties, Svoboda and Right Sector, despite being the prime bogeymen in Russian propaganda, did not make it into parliament.

The relationship between the current authorities and the opposition or, speaking broadly, the former associates of Yanukovich, is not conflict free. The Law on Lustration adopted in September 2014 envisages that people associated with Yanukovich’s regime cannot take public positions. Moreover, some MPs from the Oppositional Block are suspected to have supported the insurgent militia in Donbass and might be subject to prosecution if parliamentary immunity is lifted. The criticism of these initiatives as well as blaming the authorities for the war in Donbass are the cornerstones of the rhetoric of the opposition.

Another potential source of societal tension could be the large number of internally displaced persons in different regions of Ukraine. They are welcome all over Ukraine and numerous volunteer initiatives help them to survive and adapt. However, the fact that many young men from different parts of Ukraine have lost their lives fighting for Ukraine’s territorial integrity, while young men flee from Donbass, is not easily accepted everywhere. At the same time, many educated people forced to flee from Donbass and Crimean Tatars forced to leave Crimea have started playing an active role in politics, civil society, the media and business, throughout Ukraine.

## II. Management Performance

### 14 | Steering Capability

Ukraine’s political leadership claims to pursue long-term aims and fulfill the demands of Maidan to overhaul the political system, but this is not always the case in reality.

As of the beginning of 2015, reforms in Ukraine were guided by four different documents. First, the Action Plan for Implementation of the Association Agreement was adopted in September 2014. It contains a long list of activities covering the entire Association Agreement, ranging from reforms of political system to very technical standards. It indicates timelines for implementation and the authorities responsible from Ukraine and the EU. Second, following the early parliamentary elections in October 2014, the Coalition Agreement was adopted by the parties forming the parliamentary majority. It includes 17 reform areas, which are supposed to overhaul the entire system of governance in Ukraine. Third, the Action Plan of the Government was adopted in December 2014. It claims to be based on both documents mentioned above and refers to the Coalition Agreement as its integral part. It contains 13 priority

Question  
Score

Prioritization  
5

reform areas for the period of 2015-2016. Finally, there is the so-called Strategy 2020 – the document developed by the administration of the president, adopted in January 2015. It includes 60 priorities, covering a broad spectrum of reform areas.

The activities of the government are guided mostly by its Action Plan, which, according to civil society experts, although defining the priorities correctly, misses some important reform areas.

The government's approach to dealing with fiscal constraints is also questionable. Instead of providing for measures that would improve the business climate and ensure economic growth, it has opted for taxation measures that would bring immediate additional budget revenues. At the same time, however, the system of state control over business activity has been loosened.

Implementation of the reforms by the current government is too difficult to assess, given that the Action Plan of the Government was adopted only in the beginning of December 2014. However, looking back at the reform process starting from the end of February when the first post-Maidan government was appointed, the results are rather mixed.

Implementation  
5

With the government in place from February to November 2014, a lot depended on individual ministries. The Ministry of Education proved to be the most successful. With the help of the parliament, which passed the respective legislation, the Ministry managed to launch a reform of education that introduced the autonomy of universities and system of qualifications that meets the demands of the Bologna Process. The other ministries and the Cabinet in general did not achieve very much.

On the positive side, the government managed to reduce both the public service apparatus (28,000 civil servants were fired) and the expenses for the public service by 10%. The number of taxes was reduced from 22 to 9, while the number of authorities that exercise control over private business was reduced.

However, many other declared objectives were not fulfilled, including fighting corruption, carrying out constitutional reform to delineate the powers of the president and the prime minister more clearly, decentralization and reform of the judiciary. In some such reform areas, the necessary laws were adopted but have not yet been implemented given the short period of time. Moreover, there has been lack of transparency regarding implementation, which makes assessment difficult.

In previous periods, policy learning used to be a weak area in Ukraine. Significant policy learning resources – whether from international donors or civil society – were used insufficiently. This has fundamentally changed in the course of the Euromaidan. Many recent reforms have been adopted as the result of pressure coming from civil society and/or international donors. Although this, in itself, does not necessarily reflect improved policy learning capacities in the relevant institutions, a number of

Policy learning  
7

ministries and executive bodies have shown considerably improved skills. The Ministry of Education, for instance, led by Western-oriented university managers, is a success story. Many ministers and specialists in top positions in the new government speak fluent English and come from outside of the public sector, which was never the case previously. This gives hope that the expertise and experience from business, academia and civil society will have an ongoing impact on the work of the government.

In addition, policy learning is occurring on some levels of the bureaucracy, which have become more open to external expertise. However, the system of civil service (for instance, promotion rules) does not yet encourage application of this knowledge. As a result, policy learning has only to some extent led to a more informed and effective practice. However, the war in the east of Ukraine, the economic crisis and the demand for reforms from society and from outside provide additional incentives for the government to be innovative and more resource efficient. For instance, Ukraine managed to significantly reduce its gas consumption and increase expenditure for the army without cutting social expenses.

## 15 | Resource Efficiency

Although the number of civil servants was reduced in Ukraine in 2014, this measure is not sufficient to enhance the efficiency of the civil service in Ukraine. It still suffers from many deficiencies and full-fledged civil service reform is yet to be carried out.

Efficient use of  
assets

4

Another problem is that Ukraine still remains a highly centralized state, which negatively impacts the use of resources at local and regional levels. Although the first steps in the direction of budgetary decentralization have been taken, this is insufficient to empower local authorities and shift responsibility for solving problems on the ground from the center to the municipal level.

The fiscal situation is difficult. The consolidated fiscal deficit (excluding recapitalization) was about 5% of GDP in 2014. It would have been higher if all planned expenditure had been executed. Total state debt skyrocketed to 70% of GDP in 2014 (2013: 40%).

Budget planning procedures have been regularly violated. The Budget Law 2015 was passed just few days before December 31, 2014, and was supplemented by many tax novelties entering into force in January 2015. This was a direct violation of legal norms, as at least six months have to pass before new tax-related laws can be enacted.

The system of policy coordination somewhat improved in 2014. Due to a return to the parliament-presidential form of governance, the coalition government has better opportunities to coordinate its policy objectives with interests represented in the parliament.

Policy  
coordination  
6

Several governmental committees were established to coordinate cross-sectoral policy: on social, economic development and international cooperation; on defense issues; on regional development; and on humanitarian development.

The role of the Secretariat of the Cabinet of Ministers was strengthened, as it was restructured to ensure coordination of sectoral policies at the central level.

Moreover, a new structural unit – the Government Office for European Integration - was created to coordinate all activities of the line ministries and other executive bodies in the area of European integration. To this end, the position of deputy minister for European integration was introduced in all ministries.

Coordination mechanisms are still to be improved and the reform of public administration is defined as a priority area for Ukraine. It remains to be seen how it will be carried out.

Conflicting policy objectives, such as the need to strengthen the army, limit consumption of energy resources, limit the opportunities for misuse of public resources and meet social needs are being addressed with mixed success.

During the Presidency of Yanukovich, the level of corruption in Ukraine reached an unprecedented level. Fighting corruption was one of the major demands of the Euromaidan, and has been as a priority of the post-Maidan government and President Poroshenko (at least rhetorically). So far, the results have been meager.

Anti-corruption  
policy  
4

Several initiatives adopted to address the issue include the new law “On access to public information,” which, if implemented, is supposed to make the work of different public institutions and decision-making process more transparent. Another important new law is “On Public Procurement.” This is intended to end the policy of single-source procurement and, according to experts, will help save up to UAH 70 billion annually. In October 2014, the parliament adopted the package of laws on anti-corruption, including the anti-corruption strategy for 2014-2017 and, importantly, the establishment of the Anti-Corruption Bureau as a major body to combat high-level corruption.

Other institutional provisions include the establishment of the National Commission for Prevention of Corruption and the National Council on the Anti-Corruption Policy. The former institution is a central executive body responsible for the elaboration and implementation of the state’s anti-corruption policy. The latter institution was established as an advisory body to the president. The roles of the National Council

and the National Commission overlap in many cases. It is too early to say how these legislative and institutional initiatives will function in practice.

Finally, party financing is not transparent and not regulated by legislation; moreover there is no state funding for political parties, although the relevant law was adopted in the first reading. Such funding would enable young political parties that do not have strong financial backing to run elections and reach out to voters.

## 16 | Consensus-Building

Rhetorically, all actors are committed to the principles of democracy and a market economy. Moreover, the parliamentary coalition and the government formed by it supposedly represent the Maidan and its values. The latter stood for the overhaul of the old system of governance and a more democratic and transparent system based on the rule of law and free market competition. In reality, it is not clear to what extent all actors within the so-called “democratic camp” are really committed to these principles. The system that has always been in place in Ukraine, enabling only partial reforms and the prevalence of particularistic interests, is still there. The difference now is that there is stronger pressure from society and the international community to pursue reforms. Moreover, there are more democracy and market-economy oriented actors in the parliament and government than before. For instance, many civil society leaders, journalists and people with an international business background have become members of the parliament or have joined the government. There are also actors who are not necessarily interested in reforms. First, there are powerful actors, for instance oligarchs, who prefer the old rules of the game, including a poor business climate aimed at preventing competition from smaller domestic businesses and foreign investors, poor rule of law and a politically controlled judiciary. Moreover, the political opposition in the form of the Oppositional Block parliamentary faction, which includes mostly representatives of the former Party of Regions (Yanukovich’s political arm), abstain from voting on most of the laws adopted by the parliament, and their criticism of the authorities is not constructive. Finally, the inertia of the old system will continue to hamper reforms.

Formally, there is consensus among key political actors that Ukraine should have a market-based economy as strategic long-term goal of the country. However, there are acute debates about the ways to achieve the goal. It is expected that the Association Agreement with the EU, signed and ratified in 2014, will provide an important anchor for market-based reforms in the country and limit the space for maneuver for the actors who veto reforms.

Consensus on goals

7

For the time being, the reformers, if one considers the ruling coalition and the government to be the reformers, seem to be in the situation where they can pursue their goals if the political will is indeed there.

Anti-democratic  
actors

6

The ruling coalition has 302 seats in the parliament, representing the constitutional majority. Both the president and the government represent the same political spectrum, which grew out of the Maidan protests and was in opposition to Yanukovych. The formal opposition, which is represented by the Oppositional Block faction, has only 40 seats. This means that there are no major stumbling blocks for passing decisions. Indeed, the parliament works rather efficiently: between the end of November 2014, when the coalition was formed, and the end of January 2015, 113 laws were adopted.

However, the implementation of many reforms has been blocked at the central and local levels by the inertia of the old and ineffective system, a low capacity to implement some innovations, and resistance to implementation by different actors. Some actors who bear responsibility for the developments during Yanukovych's regime have made their way into parliament or have preserved their influence at the local level. Several corruption scandals with the new authorities have not been followed up with a court and populist actors have become stronger. Both developments undermine democratic gains achieved thus far.

The way the initiated reforms will be implemented over the course of 2015 will be the real test. This will reveal the veto-playing potential of explicit anti-reform actors. Moreover, the extent to which the current government is reform-minded will also be tested. Given that only a few months have passed since the most recent parliamentary elections and since the government was appointed, any conclusions are premature at this stage.

Two simultaneous trends can be observed in Ukraine today. On the one hand, the Euromaidan protests and subsequent Russian military intervention have united society in Ukraine. The protests against Yanukovych's rule, although significantly stronger in Kiev and the west of Ukraine, also took place in many cities in the south and east of Ukraine. This phenomenon showed that the traditional electoral cleavages - between a Ukrainian-speaking west and a Russian-speaking south and east - are diminishing further. The post-Euromaidan public opinion polls confirm this trend. According to a public opinion poll conducted by the Democratic Initiatives Foundation in October 2014, the identification with Ukrainian citizenship, as compared to regional or local identification, prevails throughout Ukraine - at a level ranging between 76% and 59%. Even in Donetsk, which finds itself outside Ukrainian control today, the largest ever pro-Ukrainian demonstration took place right after the Euromaidan.

Cleavage /  
conflict  
management

4

On the other hand, the Euromaidan and Russian aggression have aggravated the dividing line between Donbass and the rest of Ukraine. According to the same public opinion poll, only 34% in Donbass identify themselves with Ukraine and 27% identify themselves with Donbass, which is a significantly higher regional identification than in other parts of Ukraine. Moreover, 70% in Donbass think that the Euromaidan was a coup d'état, and the majority of people in those parts of the Donbass that were regained by the Ukrainian army from the insurgent militia do not consider Russia to be an aggressor. So far, the Ukrainian state has not paid attention to this problem. People in these territories feel abandoned by the state, as the authorities from Kiev do visit, while the local authorities who were in the office during Yanukovich's presidency are still present. In other parts of Ukraine, where the Maidan discourse prevails, there have been cases of intolerant and violent treatment of people associated with Yanukovich's regime, outside of the judicial process. Therefore, reconciliation is urgent but should not become a pretext for blocking political change.

In general, civil society has a limited impact on decision-making, since political leadership still frequently ignores civil society actors and formulates its policy autonomously. Ukrainian legislation foresees the formation of public advisory councils to state agencies so as to ensure civil society participation in the policy process. Of the 608 public councils envisaged at different levels, almost all were created. However, many of these councils exist only formally, and their effectiveness remains very low.

Nevertheless, it has become more difficult for political leadership to ignore civil society after the Euromaidan due to two factors. First, the events that enabled the current political leadership to take office were largely driven by civil society: the change of political elites was the outcome of the Euromaidan protests. Second, civil society has become stronger, better organized and persistent in its objective to be included in the policy process. One success story is the previously-mentioned Reanimation Package of Reforms (RPR) initiative. As a result of this, some 20 important laws advocated by the RPR were adopted between March 2014 and January 2015. Thanks to these laws, independent public broadcasting was launched, the autonomy of universities was established, the risk of corruption was reduced, and better access to information was secured, among other achievements. Some laws were passed due to activists of the initiative organizing protests near the parliament or managing to include specific reform demands in the financial conditionality of Western donors to the government of Ukraine.

Despite many success stories, the political will for reforms among the current authorities is low and the decision-making process still lacks transparency. Powerful economic actors such as oligarchs still exercise a lot of influence through informal networks. A lot of reforms that would overhaul the political system and change the old rules of the game have not yet taken place.

Civil society  
participation  
6

One of the most recent conflicts took place during the Euromaidan, and resulted in the deaths of over 100 people – mostly protesters, but also several in the police force. This conflict is still too fresh to judge. Society demands that this situation is investigated and those who gave the orders to kill and those who followed these orders be brought to justice. However, no information about investigations, if any, has been made public. Information coming from the authorities and independent investigators is contradictory.

Reconciliation  
4

When it comes to fresh conflicts, another dimension concerns the situation around Crimea and Donbass. While the Crimea is now *de facto* under the control of the Russian authorities, the fighting in eastern Ukraine has seen human rights violations and war crimes perpetrated by both sides, that is, also by the Ukrainian army, mainly because fighting takes place in highly populated areas. Due to exposure to Russian media, people in the territories that were freed from occupation do not regard Russia as an aggressor, and opinions there about Ukrainian state are divided. These fresh wounds still have to be better understood and dealt with. If Ukraine accepts the full authority of the International Criminal Court, as demanded by the Association Agreement with the EU, this issue could be the subject of trials at the Court.

With respect to historical injustices, many historical injustices in Ukraine – mostly related to Stalinist or Nazi crimes – have not yet been discussed comprehensively or systematically. The Holodomor (the state-caused famine in in the 1930s) became an exception. Although many in Ukraine refuse to recognize the Holodomor as genocide against the Ukrainian people, it has already become a tradition to commemorate this date, including at the state level.

Another problem is the status of World War II veterans who did not fight on the side of the Soviet army, but rather with the Ukrainian Insurgent Army (Ukrayins'ka Povstans'ka Armiya, UPA). This group fought for Ukraine's independence against both Soviet and Nazi forces. UPA veterans are not entitled to the same compensation as Soviet veterans; in fact, some parts of the society consider them to be war criminals and accuse them of collaboration with the Nazi forces. In addition, their alleged involvement in anti-Semitic pogroms has not been properly discussed. Nevertheless, they receive positive recognition by local authorities in the western regions of Ukraine. This topic still divides society.

## 17 | International Cooperation

After the Euromaidan, Ukraine has become a recipient of substantial financial assistance from international institutions. This includes a two-year stand-by loan from the IMF worth \$17 billion, which may be increased, and a \$1.8 billion loan from the World Bank for various projects. About €1 billion of both loans and grants has also been committed by the EU, including the European Commission, the EU member states, the EBRD and the EIB. Given the amount of funding, the diversity of modes of funding and projects, and the different conditions set up by different donors, the effectiveness of using this aid will largely depend on the availability of a strong and efficient coordination mechanism.

Effective use of support

6

So far, this has been problematic. On the one hand, the Ministry of Finance and the National Bank are mostly concerned with loans, and are primarily responsible for cooperation with the IMF, the World Bank, the EBRD and the EIB. On the other hand, the Ministry of Economic Development and Trade is the formal governmental coordinator for technical assistance and grants, which mostly come from the European Commission and the EU member states. However, the poor capacity of the respective ministries to coordinate external assistance and their limited powers with respect to other ministries has hindered effective use of external funds. An approach that would ensure that external aid matches domestic reform priorities is also absent.

The Action Plan of the Cabinet of Ministers adopted in December 2014 contains clear priorities and timelines for their implementation, but has no reference to responsible authorities and how this Action Plan should take international assistance into account. However, this Action Plan also presupposes that a Single Centre for Coordination of Donor and International Assistance is to be established.

Lack of transparency with respect to spending the external assistance has also been a problem. Civil society experts have continuously criticized the government for not providing sufficient information about international funding management, thus limiting the opportunities for civil society to monitor the implementation of assistance and to exercise independent control.

Ukraine's credibility with international actors significantly deteriorated during Yanukovich's Presidency, but renewed after the transition of power.

Credibility

6

Both post-Maidan governments under Prime Minister Arseniy Yatseniuk have enjoyed significant, yet cautious, international credibility. International financial assistance mostly includes strict conditionality. This approach is favored by civil society, since it is expected to force the government to implement reforms.

The credibility of the new government was boosted by appointment of three ministers who were not previously Ukrainian citizens, but were granted Ukrainian citizenship

to enable them to take their posts. These are the Minister of Finance Natalie Jaresko (USA), the Minister of Economic Development and Trade Aivaras Abromavicius (Lithuania) and the Minister of Health Oleksandr Kvitashvilli (Georgia). It is expected that newcomers, never previously linked to Ukraine's public authorities, will be able to reorganize bureaucratic public institutions and fight corruption.

Although international partners of Ukraine have committed significant financial support to Ukraine, the pace of reform is considered to be slow. A donor conference on Ukraine's financial issues, organized by the European Union, is expected to take place in spring 2015 to assess reform progress and meet support needs.

At the same time, there have been several incidents of human rights violations by the Ukrainian forces (such as those criticized by Amnesty International). These might have somewhat decreased the international confidence in the new Ukrainian government.

Ukraine aims at having good relations with all neighboring countries. Ukraine is a founding member of the Commonwealth of Independent States (CIS) and a member of GUAM (Georgia, Ukraine, Azerbaijan and Moldova), the Organization of the Black Sea Economic Cooperation (BSEC) and of the Central European Initiative (CEI). These organizations, except for GUAM, were founded primarily to counteract Russian influence in the region, and mostly serve as platforms for political elites to meet and exchange opinions.

On a pan-European scale, Ukraine is a member of the Council of Europe and the OSCE.

Ukraine has also expressed interest in cooperation with and even potential membership in the Visegrad group (Czech Republic, Slovak Republic, Poland and Hungary) and the Weimar Triangle (Germany, France and Poland). However, so far Ukraine has only been a subject of discussions or official statements by the two organizations.

Ukraine's relations with Russia have undergone a dramatic transformation since March 2014, when Crimea was annexed and the conflict in Donbass started. Russia failed to drag Ukraine into the Eurasian Economic Union (Russia, Belarus, Kazakhstan, Armenia and Kyrgyzstan). Although there were problems in Ukraine-Russia relations before, such as cut off gas supplies and trade restrictions, Russia had never been perceived as a military threat to Ukraine. The aggression forced Ukraine to fortify its border with Russia and boost its military power. Moreover, public opinion with respect to Russia deteriorated significantly. Whereas, in November 2013, over 80% of Ukrainian citizens and around 70% of Russian citizens expressed positive attitudes towards the respective neighboring country, in October 2014,

Regional  
cooperation  
8

slightly less than 50% of Ukrainians and slightly over 30% of Russians still had positive attitudes towards their neighbor.

Ukraine has been cooperating with many Western neighbors, particularly Poland, whose support of Ukraine's European integration has played an important role. There are cross-border cooperation projects with Poland, Hungary, Slovakia and Romania, mainly within the framework of the European Neighbourhood Policy and the Eastern Partnership. Simplified border crossing for people living within 30 kilometers of the border with Poland, Slovakia and Hungary was introduced. When Russia stopped gas supply to Ukraine in June 2014, these countries supplied gas from the EU as part of the special gas reverse arrangement.

Ukraine's cooperation with countries of the Eastern Partnership (in addition to Ukraine, the initiative includes Moldova, Belarus, Georgia, Armenia and Azerbaijan) remains intensive. Although this cooperation was and is still driven by the European Union with little initiative from the ground, it serves as a forum for socialization among officials, civil society and other actors from the six countries.

## Strategic Outlook

The Euromaidan opened up a new opportunity for Ukraine to fundamentally change the pattern of its development that has prevailed since its independence. While most politicians in the new system are representatives of the old system, many civil society leaders and professionals with a business background have become members of parliament or have taken positions in the government. This provides ground for optimism. Moreover, civil society has matured and has shown that it is not willing to give the authorities a free hand, but will rather continue to keep the authorities accountable.

Ukraine has signed, ratified and started implementing the Association Agreement with the EU. With the agreement in place, reform-minded actors have received an important boost and leverage to promote these.

However, Viktor Yanukovich and his predecessors, who either lacked political will or were incapable of introducing far-reaching reforms, have left Ukraine's post-Euromaidan authorities with a difficult legacy that is difficult to get rid of. This includes a de facto privatized state, where policy-making is driven primarily by particularistic interests, an inefficient civil service, a judiciary and law-enforcement authorities incapable of performing their tasks and dependent on political whims, a poor business climate, and an economic situation close to default.

At the same time, Ukraine's relations with Russia are expected to remain extremely difficult in the years to come. However, due to many interdependencies, Russia will continue to play an important role in Ukraine's domestic developments.

While some important reforms were initiated in Ukraine since the ousting of Yanukovich, the results so far have been meager. Hardship and a lingering reform process not only jeopardize the achievements of the Euromaidan but also lead to disappointment with the pro-European course.

It is therefore vital for Ukraine to break the reform blockade and establish democratic rules as the only game in town. This comprises several important tasks: the ruling elites need to provide a prime example of following democratic rules, including the separation of business and politics and strict implementation of transparency rules in order to fight corruption. This also includes state funding for political parties with strict rules to ensure transparent party finances and media ownership.

A (partial) change in the composition of the political elites should be promoted. Civil society representatives, young professionals and external experts should receive a greater role not just in specific reform projects but in policy-making and in political debates in general. The consolidation of the political party system should be enhanced in order to promote sustainable program-oriented parties instead of the political projects of prominent individuals.

Public debates need to become less populist. In order to achieve a sustainable consensus on needed reforms, politicians have to focus on reform projects and refrain from unrealistic promises and unfounded accusations against rivals. Not just freedom of media, but also the professionalism of journalists should be promoted. A sustainable funding scheme for think tanks and experts should also be developed.

It is also important to reform the civil service in order to separate political and bureaucratic levels and to enable young professionals with international experience to occupy important positions. Civil service reform can be enhanced through decentralization, i.e. authorities at the municipal level should receive the power and resources to meet the needs of the people. Another important step is a reform of the law-enforcement agencies and the judiciary in order to free them from political influence.

State regulation of the economy should also be freed from direct political meddling and extensive state regulation (often introduced for the sole purpose of extorting bribe payments) should be reduced.

While international promoters of reforms in Ukraine (most extremely the IMF) very much focus on the technical aspects of specific reform measures or policy adjustments, the major task is to overhaul the old system of governance. For this aim, a new generation of politicians, civil society activists, experts and journalists need to be trained, supported and promoted to decision-making positions.

Ultimately, it is these measures which will decide the very fate of Ukraine in the years to come.