

CASE - Center for Social and Economic Research



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Priorities of Economic and Institutional Reforms in Ukraine

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Key economic policy challenges

- Macroeconomic problems (slow GDP growth, inflation, fiscal imbalances, rapid credit growth, deteriorating trade and current account balance)
- Consequences of gas price shock
- Excessive and ineffective social programs
- Poor business/investment climate
- Frozen privatization & re-nationalization fears
- Need of deeper integration into the world/
European economy (WTO accession, EU-Ukraine economic relations)

Main Macroeconomic Indicators, 2000-2007:

Item		2000	2001	2002	2003	2004	2005(e)	2006(f)
GDP	growth rate %	5.9	9.2	5.2	9.6	12.1	2.6	2.4
CPI	% eop	25.8	6.1	-0.6	8.2	12.3	10.3	13.0
Exchange rate	UAH/USD eop.	5.4	5.3	5.33	5.33	5.31	5.05	5.05
Current account	bln. USD	1.5	1.4	3.2	2.9	6.9	2.5	-8.7
Budget deficit	% of GDP	0.6	0.3	-0.7	0.2	2.9	1.8	3.6

eop. - end of the period

Source: State Statistics Committee of Ukraine, NBU, CASE Ukraine estimates

Premature post-communist welfare state

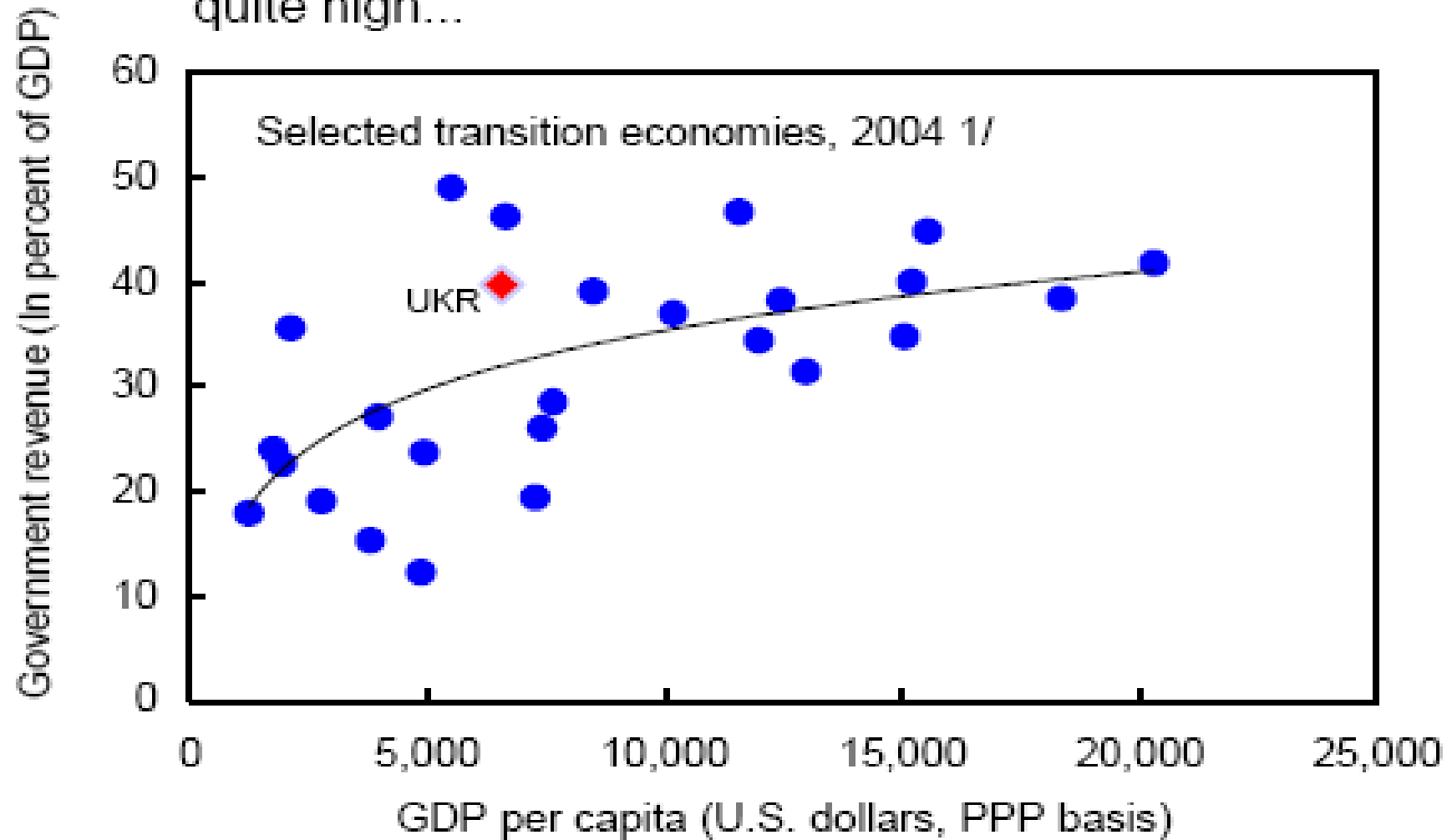
- Burden of social privileges inherited from the Soviet period and first years of independence
- Pension system: very low effective retirement age and overly generous system of disability pensions (⇒ high dependency ratio)
- Highly unfavorable demographic trends ⇒ further rapid deterioration of pension fund balances
- Eruption of social populism during and after the Orange revolution
- Negative fiscal and microeconomic consequences

Recent dynamics of social expenditures (2004-2005) in % of GDP

Item	2003	2004	2005 est.	2005-2003
GG expenditure	36.8	39.4	42.7	5.9
transfers total	14.8	16.7	21	6.2
transfers to PF	9.1	11.3	14.9	5.8

Source: *IMF Country Report No. 05/415 Table 3, p.39*

As a result, Ukraine's revenue-GDP ratio is now quite high...



Source: *IMF Country Report No. 05/415 Figure 3, p.12*

...and the pension spending-GDP ratio is one of the highest in the world.



Source: IMF Country Report No. 05/415 Figure 3, p.12

Key determinants of unfavorable business climate

- Barriers of entry (registration and licensing regime)
- Legal system, its stability and transparency
- Law and contract enforcement, protection of property rights
- Quality of state institutions, including civil service and judiciary, role of law enforcement agencies
- Tax system and administration
- Underdevelopment of financial sector and low quality of financial services
- Underdevelopment and monopolization of infrastructure

Privatization/ re-nationalization

- Slow/ moderate speed of privatization in the past; non-transparent rules of large privatization
- Post-revolutionary reaction: a lot of ownership / re-nationalization claims resulting in deterioration of investment climate
- Krivorozhstal tender gave chance to restart a large privatization on a transparent basis but also created temptation to continue re-nationalization claims
- Many enterprises still state-owned

Trade and economic integration:

- the forthcoming WTO accession (it could happen faster);
- necessity to plan the next steps (EU-Ukraine trade liberalization) in advance on both sides;
- limited effects of classical trade liberalization
⇒ need of “deep FTA” or “FTA Plus”
- adjust FTA with CIS countries to WTO rules