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International
Centre
for Policy
Studies

4 Borys Hrinchenko st., office 3, Kyiv, 01001, Ukraine
Phone (380 44) 279-88-23 | office@icps.kiev.ua | www.icps.com.ua

Inside Ukraine

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The Government Policy

It has been a year since the beginning of Euromaidan but the culprits and ringleaders have not been prosecuted. Poor coordination between the investigating authorities of Prosecutor General's Office, Security Service of Ukraine and the Ministry of Interior, as well as politicization of the process, casts doubts on establishing justice and ensuring inevitable punishment of criminals. Meanwhile, on November 24 in Kharkiv, the first court judgement appealed against the Law of Ukraine "On purging the government bodies".

Dismissed prosecutor was reinstated and a legal precedent was created.

While the Ukrainian side slams the format of negotiation and the government withdraws from settling the situation in Donbas, quasi-republics "DPR-LPR" continue to legalize their institutions. The Kremlin convinces the international community that the war in the East is a conflict between Kyiv and Donetsk. Official Kyiv is lacking in comprehensive negotiation package and, thus, vision of tactics and strategies for conflict resolution.

Political corruption shields ringleaders of crime on Maidan from punishment



After the fall of Yanukovich's regime, the transitional authorities did not implement structural reforms, particularly in the field of justice and law enforcement. Therefore, the law enforcement officers, who were personally involved in repressions against protestors, investigated crimes on Maidan. The investigation was obstructed at political level, since already in February the society knew which policemen and senior officials were directly related

to crimes. Absence of political determination and presence of corruption in the investigation process discredit the ability to bring ringleaders and culprits to justice. Failure to carry out reforms diminishes nationhood. Corruption of officials and law enforcement representatives led to rampant separatism in Crimea and Donbas.

None of the culprits has been brought to justice

Lustration process has been gradually discredited in the eyes of the public and international community. The Law of Ukraine “On purging the government bodies” is inconsistent with other legal acts and provokes a number of legal collisions. The lawmakers and civic activists have not taken into consideration all peculiarities of Ukrainian legislation, as well as experts’ suggestions of possibility to appeal against dismissal of people under lustration law in court.

The Law of Ukraine “On purging the government bodies” is inconsistent with other legal acts and provokes a number of legal collisions

As an example, on November 24 in Kharkiv, the first judgment of the court reinstated Volodymyr Suhodubov, a head of personnel department of the

Kharkiv Regional Prosecutor’s office. The official was fired on October 23, but exactly in one month, Themis resumed chief human resources officer’s rank and position. The court read out only the resultative part of the decision without legal justification, but this judgement established a precedent. Volodymyr Petrov, a chief prosecutor of Sumy region, follows the similar procedure in an effort to resume his position, from which he was dismissed by PGO order of 23 October 2014.

Lustration process was bound to fail because the judiciary is not reformed and regarded as the last outpost to back up corruption. Lustration of state institutions and law should become the priority goal of the parliament.

Ukrainian courts require reforms and judiciary renewal

The self-proclaimed republics actively legalize

Kyiv withdrawal from resolving problems in Donbas unleashes separatists who set up a militarized zone of quasi-public institutions with the Kremlin support. Despite the Ukrainian government’s refusal to recognize DNR and LNR legalization, the self-proclaimed republics resume the work of government bodies, health care, education and try to organize the tax structures.

Kyiv withdrawal from resolving problems in Donbas encourages separatists to legalize quasi-public institutions

In the nearest future “DNR-LNR” will launch the legislative bodies, people’s parliaments, which will comprise 100 deputies each. By 15 December 2014 separatists plan to complete reregistration of budget property, social and community establishments in controlled areas. Absence of cash flows and financial blockade from Kiev encourages separatists to introduce their own currency. There are already samples of quasi-republics People’s Bank notes on the Internet.

The self-proclaimed head of DNR Oleksandr Zakharchenko has announced that at the beginning of 2015 the Constitution is expected to be adopted and elections to local governments to be held. DNR is trying to restore the banking system,

in which the People’s Bank will carry out the central bank functions. In Sverdlovsk, which is controlled by LNR, the Tax Service has started the paid re-registration of legal entities and entrepreneurs by threatening penalties.

These are the first joint steps of the Kremlin and militants designed to legalize separatist units. Accumulation of Russian military equipment and manpower is observed in the occupied territories, which indicates the enemy’s intention to attack or strengthen the defense. In response to “DNR-LNR” actions, the Ukrainian side has launched the construction of a three-tiered line of defence.

The conflict in Donbas develops under Transnistria scenario. Besides the formation of unified administrative vertical, an integrated command centre of militants and the Russian army is being created for coordination. Not recognized republics “DNR-LNR”, with a population of about 4 million people, risk to turn into the humanitarian and economy collapse zone.

Stabilization and boundary alignment are across the front lines

Ukraine should handle the conflict at three levels: geopolitical “US-Russia”, bilateral “Russia-Ukraine” and intra-Ukrainian. If the first two levels are in the

competence of diplomats and the President Petro Poroshenko, the third level of conflict resolution depends on coordinated work of government and Verkhovna Rada of Ukraine. The newly elected par-

liament should create legislative environment to reduce social tension in the regions, conduct reforms and minimize corruption.

Economic Situation

The war in Donbas and the absence of necessary economic reforms keep worsening Ukraine's economic conditions month after month. According to IMF forecast, economic decline will reach 6.5% by the end of the year. EBRD projects a 9% fall, while the World Bank improved its forecast last week and put an economic decrease estimate for three quarters at 3.6%. According to the World Bank, GDP

will fall by less than 8% by the end of this year.

Ukraine is interested not only in increasing the import of Norwegian gas, but also in the development of technical cooperation and implementation of investment programs. Ukrainian-Norwegian cooperation goes beyond gas partnership, adding cooperation in nuclear energy to the portfolio of joint projects.

Economic situation during January-October 2014



Prime Minister Arseniy Yatseniuk stated that Ukraine's GDP fall might reach 7% this year. NBU projects 7.5% GDP fall.

Thus, there is a general downward trend in Ukraine's GDP fall from 6.5% to 9% by the end of the year.

**General forecast
of GDP fall by the
end of this year
is from 6.5% to 9%**

Production downturn slowed down to 16.3% (16.6% in September) due to reduced fall in mining industry. During the period of January-October 2014, Industrial Production Index was 90.6%. The improvement in the extraction of metal led to reduced production decline, with the production decline reaching 7.4% in October compared to 17.3% decline in September. Also, there was a decrease in

metallurgy industry to 21.1% in October compared to 28.3% in September. At the same time, coal extraction was hampered due to the suspension of activities in most Donbas mines. In October, coal extraction reached 60.5%.

The decline of process manufacturing slightly accelerated and reached 12.4% in October compared to 11% in September. Coke and oil products production (a slow decline from 52% to 42.7%) and mechanical engineering (a fast decline from 22.8% to 26.1%) keep decreasing. The biggest decline was reported in ATO zone; in Luhansk region the Industrial Production Index fell by 80% in October and by 55.2% in Donetsk region.

Traditionally the period of January-October is characterized by a slow growth of agricultural pro-

duction. As expected, this year agricultural production rose by 7.5% compared to 16% in the same period in the previous year. However, it is agricultural production output that led to the improvement of GDP forecast by a number of organizations.

Consumer price index and currency devaluation are also critical. Consumer price index rose by 19%. According to the NBU, consumer price index will be at 25% at the end of the year.

According to the NBU forecast, consumer inflation may reach 25% at the end of this year

At the beginning of 2014, currency devaluation was at 80% due to the implementation of unpopular, yet necessary, reforms as well as disbalance on Ukrainian currency market due to accumulated for the last years external disbalances.

By the end of this year the situation with Ukrainian currency devaluation and gold and currency reserves may worsen. The reason for that is the need to repay debts to Russia and an increasing burden on state budget. Ukraine has to repay USD 1.6 billion out of USD 3.1. billion in debt to "Gazprom" (USD 1.5 billion in debt has already been paid off) for Russian gas under Brussels agreements as of October 30. This debt will be served through gold and currency reserves, the amount of which was USD 12.5 billion as of November 1, 2014.

Under such conditions, Ukraine is in dire need of international financial assistance. In general, in 2014 Ukraine received \$ 8.6 billion in loans from international organizations. In the meantime, Ukraine paid off \$ 9.1 billion in debts. The largest loan was received from the IMF. However, the last IMF mission to Ukraine was not pleased with the way reforms were being implemented in Ukraine. The implementation of reforms was the main requirement Ukraine had to meet to receive the IMF loan. As a result, the allocation of IMF third and fourth tranches to Ukraine is open to question. The expected sum of IMF third and fourth tranches totals USD 2.8 billion. If Ukraine does not receive this money and economic and political situation keeps deteriorating, Ukraine may face default.

In general, economic situation will keep deteriorating over the next month. The main expected trends are:

- Increase of military expenses in relation to an actual continuation of military actions;
- Further fall in investment, decrease in exports and production fall;
- Lack of credit resources due to little likelihood of the next IMF tranche by the end of this year;
- The need to repay considerable part of gas debt to Russia.

Prospects of Ukrainian-Norwegian cooperation in energy sector

As of today, Ukrainian-Norwegian gas cooperation is successful. On October 1, 2014, PJSC "Naftogaz of Ukraine" and Statoil signed the agreement on gas supplies worth 12-15 million cubic meters of gas per day, or 8 billion cubic meters per year. The cost of Norwegian gas on Ukrainian border is USD 340 per thousand cubic meter. Such price is not very different from the one at European selling points, which vary from USD 291 to 361 per thousand cubic meters (as of October 5, 2014).

It should be noted that both Ukraine and Norway are interested in stable reverse gas flows and Norwegian gas supplies to Ukraine. Firstly, gas supplies by Statoil through Slovak gas corridor and reverse gas flows from Europe are important for Kyiv in winter time. Secondly, European countries

get the possibility to intensify the development of gas pipelines and interconnectors infrastructure, which in the long run will allow for making European gas transport system more flexible and mobile as well as less dependent on Russian gas. Technical transformations and innovations in Eastern European gas transport system may allow for supplying Norwegian gas to Moldova via Ukraine in the event of the blocking of gas supplies to Moldova and Ukraine by "Gazprom".

The recent visit of Norwegian Prime Minister Erna Solberg to Ukraine on November 18, 2014, was another argument in favour of the intensification of cooperation between Ukraine and Norway in the future. During the official visit, an inter-governmental agreement on the support for Ukrainian

state budget worth more than USD 15 million was signed. It should be noted that the parties also signed the Agreement on cooperation in nuclear and radiation safety between the State Nuclear Regulatory Inspectorate of Ukraine and Norwegian Radiation Protection Authority. In view of 95% dependence of Ukraine on Russian gas to provide Ukrainian nuclear power plants with gas, cooperation with Norway in nuclear energy is the first step towards energy independence. Earlier, Ukraine signed an agreement with Russian nuclear fuel cycle company "TVEL" to build a plant of nuclear fuel in Kirovograd region where Ukraine would be able to refine and enrich Ukrainian uranium for national nuclear power plants. However, this project did not go beyond the creation of the statutory fund and project documentation. Thus the issue of Ukraine's nuclear safety remains topical. Norway with its strong nuclear potential is a good partner for Ukraine.

New horizons of Ukrainian and Norwegian cooperation

Also, Ukrainian Prime Minister invited Norway to join an investment project on Ukrainian GTS and underground gas storage facilities. According to Arseniy Yatseniuk, Ukrainian government is ready to pass a special law to solidify Ukrainian-Norwegian gas partnership if Norway is willing to do so. There is little likelihood that Statoil might be interested in

investment projects and leasing of Ukrainian GTS due to a number of factors. Political instability, economic deterioration and gradual introduction of the state of emergency in energy sector by Ukrainian government keep out potential investors. In addition, Statoil's main clients are based in Western Europe. That is why Statoil transports gas to its clients though the North Sea shelf, whereas supplies to Eastern Europe are insignificant. Thus, Statoil top management is not interested in the development of Eastern European gas transport system.

Statoil road map for Ukraine

It is expected that Norway might be interested in cooperation with Ukrainian gas and oil companies. Cooperation between Ukrainian and Norwegian companies is beneficial in terms of technical maintenance of already designed oil and gas wells as well as of those that are almost exhausted. Norwegian companies have successful experience in the development of similar oil and gas wells. Also, they have good compressor equipment. Cooperation between Ukrainian and Norwegian producers in drilling technology and hydrocarbons extraction at the depth of more than 5000 meters may be also fruitful. It is also expected that Statoil may get interested in the leasing of Ukrainian gas storage facilities, which would allow for increasing Statoil presence in Eastern European gas market.

Political competition

Despite the victory of democratic forces and formal similarity of electoral programs, the new coalition will be unstable. In majority there are already contradictions as to economic and financial interests of oligarchic groups that have influence on parliamentary factions and deputy groups.

The implementation of government decisions ultimately depends on effective, legally protected

state apparatus and its ability to work consistently without orientation towards party and business elites. The distribution of government portfolios will affect political forces configuration and change the existing game rules of political competition. The decision to establish the institution of State Secretary may alter the present balance of power.

Shaky coalition of Democrats



Having signed the coalition agreement, the parties have focused on the distribution of government portfolios and parliamentary committees. The new coalition will be unstable because all democratic parties will compete for two major resources — access to power and influence on the allocation of budget pie.

The new coalition will be unstable

Despite the fact that the draft coalition agreement was initialled by all five parties, except for the Opposition Bloc, the search for coalition formats will be relevant during the whole term. Rivalry between the party of war “People’s Front” and the party of peace “Bloc of Petro Poroshenko” will be growing. Already now, the public witnesses protracted negotiations over the ministerial posts, es-

pecially in the Ministries of Interior, Finance and Justice. “Samopomich”, which stands for reforms and slams the party quota principle of allocating seats, will occupy a separate ideological niche in the new parliament.

For the first time in history, communists did not get into the parliament. However, the left-wing ideology will be represented in parliament. “Batkivshchyna”, the Opposition Bloc and the Radical Party of Oleh Lyashko have very pronounced centre-left platforms. These three parties will probably fight for opposition niche and ability to

The Opposition Bloc, the Radical Party and “Batkivshchyna” will fight parliamentary committees of opposition

control the Budget Committee. This fundamental parliamentary unit may be given to command of opposition forces.

Coalition alliances are highly likely to be formed and then disintegrated. In any case, the coalition will be created from two largest parliamentary units, one of which is oriented to the President and the other to the Prime Minister. Arseniy Yatsenyuk will show off his political ambitions and pursue aggressive policy for the sake of his future career. In the light of the President's falling ratings, this is the most plausible scenario. Since Yatsenyuk held office as Minister, Speaker of Parliament and Prime Minister, presidency is the final stage in his career advancement in the civil service.

Smaller parties, parliamentary groups and units that can form ad hoc and interest groups will become additional players in the government. For example, in the Parliament of the 8th convocation there is a powerful agricultural lobby which will try to tackle land and food issues. For such subjects the cooperation with the Prime Minister will be profitable because the government offers access to most resources and posts.

Parliamentary groups formed from majoritarian candidates will become strong situational players

The confrontation between the President and the Prime Minister may lead to the crisis of power, as it was in 2008-2009. Recurrent conflicts will become a dominant feature of the new government.

State Secretaries as a plausible tool for presidential control over ministers

On the anniversary of Euromaidan MPs signed the coalition agreement which top priority is to reform the public administration. Deputy factions which took part in the coalition formation applied the International Centre for Policy Studies idea for introducing the institution of State Secretary. However, analysis of the coalition agreement indicates that not all experts' recommendation were taken into account.

Signed by a parliamentary majority document does not provide a precise mechanism for differentiation between political and administrative offices in the central authorities. "Bloc of Petro Poroshenko" representatives proposed to introduce State Secretaries of government and ministries. The agreement does not specify who will appoint Secretaries of State and how they will be protected from party interference.

The agreement does not give the authority to State Secretaries to manage civil servants corps

Alternatively, it is offered to form typical secretariats of ministries and other central executive bodies, which will most probably carry out clerical work and will be suspended from the human resources management. There is a considerable risk that the Presidential administration employs the institution of State Secretary as a political instrument to control

and manipulate ministries who represent other parties. Of course, in Ukrainian realities the coalition agreement is not a document of last resort, however, the agreement content raises a lot of questions.

In most democratic countries, the organization of ministry management is representative. Minister politician, who has one or more political deputies, is appointed, and there is State Secretary of the Ministry, a career official who is responsible for administrative management of the ministry. There are differences in job titles but the principle of organizing the ministry is the same. Such a model allows the parliament to implement political programs through the government, while the state apparatus is protected from political rearrangements if a new President, head of government or political minister comes into office.

The institution of State Secretary is a top of civil servant career and requires a number of competences and skills

The structure of the central executive bodies has to initiate a "political bloc" which will comprise the Minister, political Deputy and Patronage service, as well as "professional civil service" bloc headed by the Secretary of State. This office should be appointed on professional grounds and be protected from the party interference by law.

The aim of the publication is to provide objective information on current political events in Ukraine and thorough analysis of major tendencies in domestic politics. Such analysis will assist in setting priorities in the process of implementing reforms in Ukraine and in evaluating quality of state decisions from the viewpoint of their impact and sustainability. Special attention is paid to evaluation of political competition in Ukraine and ability of key political players to address challenges.

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Idea of the project: Vira Nanivska

Responsible for the project: Iaroslav Kovalchuk

Responsible for the chapters:

The Government Policy — Anatoliy Oktysyuk

Economic Situation — Vasyl Povoroznyk

Political Competition — Anatoliy Oktysyuk

Team of ICPS experts:

Vira Nanivska, Iaroslav Kovalchuk, Vasyl Povoroznyk, Angela Bochi, Anatoliy Oktysyuk, Olena Zakharova, Volodymyr Prytula, Vasyl Filipchuk.