



Guest post: economic reform in Russia's shadow

By Dalibor Rohac

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Beside the professional security in front of the building of Ukraine's Cabinet of Ministers, a small group of volunteers from the Maidan is holding guard, a reminder that the political elite is there to serve the people, not the other way round. Inside, in a quintessentially post-Soviet boardroom with heavily draped windows and photographs of stern-looking former Ministers, a senior government official tells our group that they are "a government of kamikazes."

He was not referring just to the Russian threat that is palpable in the country. Ukraine's military forces are practically non-existent – a fact that Vladimir Putin, Russia's president, has already exploited in Crimea. At the same time, Ukraine's government faces the enormously difficult challenge of saving the Ukrainian economy from bankruptcy and of delivering on people's expectations of a radical departure from the country's post-Soviet past.

"Everybody knows we are on a kamikaze plane so there is little else for us to do but to try and hit the target," the official tells us. Starting in April, the government is increasing natural gas prices for households, currently heavily subsidised, by 40 per cent.

While a portion of the blame for the price increase will go to Putin, who is ending the discount that Ukraine has enjoyed on its imports of natural gas from Russia, the increase will certainly be unpopular, especially among poorer households. Yet, to avoid a default, there is no alternative to a rapid reform of Ukraine's unsustainable and wasteful subsidy system. Besides households, who are receiving natural gas at some 30 per cent of its full price, an arbitrary system of subsidies targets selected companies, typically with good political connections.

The new Ukrainian government realises that fiscal consolidation is inevitable. The people, however, expect it to do much more than just bring public spending under control. The country performs terribly on measures of corruption and the quality of its institutions. While various anti-corruption laws exist, says Ksenia Lyapina, a parliamentarian, they are being disregarded. "The common mentality is to bend the rules in whatever way you want."

Indeed, many foreign businesspeople who are present in the countries of the former Soviet bloc, including in Russia, avoid investing in Ukraine because corruption there is less predictable than elsewhere, creating a huge source of uncertainty. While Russia has eleven IKEA stores, Ukraine is still waiting for its first one. The government has a long way to go in making the country

attractive to investors, by cutting red tape, simplifying the tax code, and ensuring that entrepreneurs, foreign or domestic, do not have to worry about arbitrary harassment by the government.

But change is in the air. On his recent visit to the US, Prime Minister Arseniy Yatsenyuk flew in economy class, and the Minister of the Economy, Pavlo Sheremeta, takes the metro to work. More significantly, the new government imposed a moratorium on all public procurement until new legislation is passed, which will ensure that government purchases of goods and services are done through competitive and transparent tenders.

Ordinary Ukrainians remain apprehensive. That is hardly surprising given their past experience with predatory governments. The Maidan is still on, kept running by a core group of volunteers camping on the square, in spite of the calls by some government representatives to end it. Just like the volunteer force guarding government buildings, it will likely remain in place as a reminder of the revolution until Ukrainians regain a greater degree of confidence in their government. In the future – unless it degenerates into a mob – the Maidan could play a hugely beneficial role as a watchdog organisation and as a platform for civil society.

Another reason for apprehension is obvious. Russia is flexing its military muscles on Ukraine's eastern border, suggesting that Putin's appetite might extend beyond Crimea. While the future of south-eastern Ukraine is surrounded by uncertainty, one can only hope that – as in Georgia a few years ago – the threat from the Kremlin will serve as a catalyst for much-needed economic reforms and institutional change.

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