AGENDA FOR UKRAINE

Free Market Road Show Kyiv, 2016

Володимир Федорин
24.05.2016
Ukraine is 162nd in the 2016 Index of Economic Freedom (Heritage Foundation)
PERSISTENT CORRUPTION

Ukraine is 130th in the Corruption Perception Index (Transparency International)
Ukraine is the 2nd poorest country in Europe with GDP per capita $2004 in 2015 (IMF)
UKRAINE AND ITS NEIGHBORS

Bulgaria
Poland
Russia
Turkey
Ukraine

0
5
10
15
20
25
30

DIVERGENCE INSTEAD OF CONVERGENCE

Ukraine and Its Neighbors - 1992

GDP per Capita ($, based on PPP, Russia’s is 1)

<table>
<thead>
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<th>Country</th>
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Ukraine and Its Neighbors - 2015

GDP per Capita ($, based on PPP, Russia’s is 1)

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UKRAINE  POLAND  BULGARIA  TURKEY  RUSSIA
UKRAINE  BULGARIA  TURKEY  RUSSIA  POLAND
REFORM SPEED IS INSUFFICIENT

Reform’s Speed Was Fast Enough (value of the Index 2+) Only Thrice in 33 Periods of Appraisal
...AND POLITICAL SYSTEM IS SUFFERING
Electoral Support of Center-Right and Populist Parties in Rada
POLITICAL CYCLE OF SLOW REFORMS

NEW GOVERNMENT WITH REFORMIST AGENDA

SNAP ELECTIONS, RADICALIZATION OF REFORMIST AND POPULIST AGENDA

PIECEMEAL REFORMS WITHOUT GROWTH

DISCONTENT GROWS WITH POPULIST BACKLASH
WHAT SHOULD BE DONE?!
LAND OF DREAMS

• The fastest growing economy in Europe, one of the most dynamic countries in the world
• Intensive development of infrastructure
• New system of health care, clinics and hospitals compete for customers
• New higher education system: money follows a student, zero corruption in universities
• Strong financial system that allows citizens to save efficiently, and entrepreneurs to attract investment
• Strong social system that provides a decent standard of living to those who are not able to take care of themselves
• Strong pension system, consisting of a decent basic pension and an opportunity to save freely through various financial instruments
PRINCIPLES OF THE NEW AGENDA

CURRENT APPROACH
• Compromises due to political constraints
• Cajoling existing constituencies and groups of interests
• Preservation of the ossified state apparatus, low salaries in public administration

NEW APPROACH
• Drafting reforms as if there were no political constraints
• Appealing to broad popular base and outside groups (e.g. foreign investors)
• Drastic downsizing of bureaucracy, hiring new professionals
GOALS OF THE NEW AGENDA

• DEPOLITIZATION OF ECONOMIC DECISIONS THROUGH:
  • DOWNSIZING THE STATE
  • FOCUSING ON CORE GOVERNMENT FUNCTIONS – DEFENSE AND RULE OF LAW
  • PRIVATIZATION OF ALL STATE ASSETS

• CREATING OPEN ACCESS ORDER
  • ELIMINATION OF CORRUPTION IN CORE GOVERNMENT INSTITUTIONS
  • EMPOWERING CITIZENS
  • CUTTING RED TAPE TOGETHER WITH SCORES OF GOVERNMENT AGENCIES
TOOLS FOR THE NEW AGENDA

• DEEP LIBERALIZATION
  • TAX AND CAPITAL AMNESTY
  • LEGALIZATION OF GREY ZONE ACTIVITIES
  • CUTTING SUPERFLUOUS REGULATION TOGETHER WITH REGULATING AGENCIES

• IMPORT OF INSTITUTIONS
  • RECOGNITION OF PHARMACEUTICAL, CONSTRUCTION AND OTHER STANDARDS ADOPTED IN ADVANCED ECONOMIES
  • OUTSOURCING LAST JUDICIAL INSTANCE IN COMMERCIAL DISPUTES
  • OPENING MARKET FOR FINANCIAL COMPANIES FROM OECD COUNTRIES

• NEW TECHNOLOGIES
SCOPE OF THE NEW AGENDA

LAND REFORM
Tax reform.
Lowering taxes on labor to 20%.
Abolition of corporate tax

State for businesses

TRANSPARENT PRIVATIZATION
New public service

POLITICAL REFORM
FIGHT AGAINST CORRUPTION

MILITARY REFORM
NATO STANDARDS

Customs reform. Unification of import duties (0% - for most goods).

PUBLIC SERVICE

FREE MOVEMENT OF CAPITAL

JUDICIARY REFORM

State for citizens

PENSION REFORM

State for businesses

Liberalized Labor Code

EDUCATION REFORM

HEALTHCARE REFORM

PUBLIC FINANCE REFORM
Reducing government spending to 30% of GDP
**PROBLEM**
- Ukraine is 70th among 102 countries in the 2015 Rule of Law Index
- Ukrainian court system is even less trusted than notoriously corrupt law enforcement agencies

**BACKGROUND**
- Judicial system is politicized and controlled by the executive branch
- Some judges are entangled in corrupt networks

**SOLUTIONS**

1. **Fast Overhaul of the System**
   - Establishing a single court of cassation, eliminating high specialized courts
   - Introducing the unity of courts of general jurisdiction, having withdrawn administrative and economic courts from this system
   - Consolidating court districts that may not coincide with the system of administrative-territorial division of the country
   - Conducting a transparent competitive selection of judicial candidates, giving preference to young lawyers with unblemished reputation

2. **Attracting reputable lawyers from abroad**
   - “Hybrid” procedure with distinguished foreign judges as jurors
   - Constitutional amendments allowing foreigners to hold positions in Ukrainian judiciary
   - Outsourcing appellate jurisdiction for commercial disputes

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**Ukrainian court system is even less trusted than notoriously corrupt law enforcement agencies**
## Public Finance Reform

### Problem

- Ukraine experiences systemic fiscal problems, implements the 9th IMF program,
- The level of state expenditures (43% of GDP in 2015) is too high

### Background

- State finances public premises, not services.
- Premature welfare state (pension expenditures about 15% of GDP in 2014)
- Budget is a large source of funding for the corrupt political system

### Solutions

1. **Downsizing State Intervention**
   - Reforming so called “social sectors”, especially healthcare and education.
   - Transferring financial responsibility for primary and secondary education to the municipal level.
   - Creating competitive marketplace in healthcare and higher education
   - Eliminating all state subsidies to businesses including tax benefits

2. **Open Budgeting**
   - Transparency at all stages of budget process – from planning to procurement
   - Performance-based budgeting instead of cost-budgeting

3. **Checks on Fiscal Expansion**
   - Introducing more complicated procedure for raising taxes (e.g. through referendum)
   - Introducing ceilings for public debt (50% of GDP) and budget deficit (2% of GDP)
PROBLEM

- Ukraine is the 130th in the world in terms of effectiveness of the state
- It lacks capacity to run 3500 companies
- Losses of state enterprises in 2014 amounted to 6% of GDP

BACKGROUND

- Politicians are not interested in transparent privatization
- Public opinion is against privatization (experience of 1990-s)
- Artificial preservation of monopolies in some sectors

SOLUTIONS

1. Restructuring of State Property Fund
   - Creating Agency for Privatization
   - Creating Agency for Managing State Companies
   - Transferring all state companies to the Agency for Privatization from the ministries

2. Reducing the list of companies that can’t be privatized
   - Opponents of privatization should demonstrate reasons why a company can’t be privatized
   - All other companies should be removed from the list of state assets that should not be privatized

3. Rapid and transparent privatization
   - Small and medium-sized state companies as well as assets of bankrupt enterprises should be sold via e-auctions in 6-18 months
   - Big companies should be sold with help from foreign advisers in 3-4 years
Land Reform

PROBLEM

- Private owners of 75% of Ukrainian arable land may not sell or use it as collateral and have to rent it out cheaply
- Large agricultural companies are mostly short-term investors

BACKGROUND

- Politicians and large landlords block any move forwards
- Agrarian companies lack funds for buying land from its owners
- Urban dwellers tend to patronize their fellow citizens in the countryside

SOLUTIONS

1. Lifting Moratorium on Selling Agricultural Land
   - Auctions to sell state owned land tracts in order to obtain price benchmarks
   - No restrictions on the size of land holdings owned by a person or a company should be imposed
   - No restrictions on foreign ownership of arable land

2. Privatization of all state assets in agriculture
   - Fast distribution of land plots that should legally be transferred to the current and retired employees of state farms
   - Auctioning of all state assets in the agricultural sector

3. Financial deepening
   - Liberalization of access for financial companies and banks supervised by regulators from OECD countries
   - Full liberalization of capital flows
e.Auction 3.0

PROBLEM
- Standard auctions restrict participation
- Due to the centralized architecture budget expenditure for support grows exponentially
- Problem with info accessibility

BACKGROUND
- Complicated procedures leave ample space for discretion
- As auction modules are run on a central server the chance of manipulation and misuse rom the system administrator is high

SOLUTIONS

1. Privatization and lease of state property
   - Emerging, innovative models which offer the latest technological solutions
   - Decentralized blockchain technology
   - Private trading platforms participate, advertise and attract interested parties

2. e.Auction 3.0
   - All information about auction is in permanent free access online
   - Post-moderation provides control for transparency of auctions and fairness of decisions
   - Secure management of processes due to decentralized database

3. System allows to:
   - Control budget spending
   - Minimize the existing corruption, manipulation and mismanagement risks
   - Rebuild trust in government asset management
SLAVA UKRAYINI!