



Tymoshenko Resets Ukraine-Russia Relations

Russia and Ukraine were the latest countries to hit the “reset” button after a fruitful meeting between Russian Prime Minister Valdimir Putin and his Ukrainian counterpart, Yulia Tymoshenko, in Moscow. The two leaders successfully ironed out energy related issues and agreed deeper cooperation in engineering, aerospace and space sectors.



▲ Mending fences: Russian Prime Minister Valdimir Putin with his Ukrainian counterpart Yulia Tymoshenko.

Last week's intergovernmental meeting was a major step forward in Ukrainian-Russian relations. Importantly, it enabled both countries to stabilise their new energy relationship, which took a temporary setback in March when Russian diplomatic feathers were ruffled by the EU pledging €2.5 billion to help modernise Ukraine's ageing gas transportation network. As Ukraine's sole provider of gas to Europe, Russian officials, at the time, felt marginalised by the deal.

Understanding Russian concerns, Ms Tymoshenko repeated her position that the modernisation programme would involve the cooperation of Russian companies. “We have invited Russia as one of the main partners to modernise the Ukrainian gas transportation system. I think that such modernisation can be conducted jointly,” said Ukraine's premier.

Significantly, the two leaders revisited the conditions of the 10-year gas contract signed last January. Under the deal, Ukraine was obliged to purchase 5 billion cubic metres of natural gas in the first quarter of 2009. However, consumption of gas by Ukrainian industrial customers was down 50 percent on the quarter year on year – with a total of only 2.6 billion cubic metres of gas consumed. This drop in usage was largely attributable to the economic downturn, and raised the prospect of Ukraine facing potential penalty fines in excess of a billion dollars.

Mr Putin agreed to waive the fines saying, “These sanctions are not being applied.”

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Ms Tymoshenko thanked Mr Putin. “I also want to express my gratitude for coming to agreement on the contractual clauses according to which Ukraine is to accept the contracted amounts of gas.” Also, Ukraine's premier said that her country would prepare a long-term



contract with Russia on nuclear energy co-operation. Russian support is being sought to help complete the building of two reactors at Ukraine's Khmelnytsky nuclear power plant.

"It is good that we are developing cooperation, leaving behind the period when our relations were marred by confrontation," said Ms Tymoshenko.

The talks also focused on bilateral trade, where, despite the economic downturn, trade between the two countries increased late last year and early this year, hitting the \$40 billion mark. The two countries renewed pledges of cooperation; most notably in the engineering and aerospace sectors where there are long-established ties. A satisfied Mr Putin said, "What very much pleases me is that cooperation between certain rather sensitive and important industries and enterprises is not being destroyed but deepened."



▲ Deputy Prime Minister Hryhorii Nemyria with Prime Minister Yulia Tymoshenko. The premier was also accompanied by Minister of Fuel and Energy Yuriy Prodan, Minister of Industrial Policy Volodymyr Novytskyy, Minister of Agriculture Yuriy Melnyk, Minister for Transport and Communications Yosip Vinsky and Deputy Head of Naftohaz Ihor Didenko.

Although the talks did not result in confirmation of a \$5 billion loan from Russia to help prop up Ukraine's economy, dialogue on the issue was nevertheless kept open.

The workmanlike nature of the talks indicates that Ms Tymoshenko is someone the Russians can do business with and who has the respect of the Russian leadership. Mr Putin described their meeting as "businesslike and open."

Vitaliy Bala, Director of the Agency for Modeling Situations, was quoted in the *Kyiv Post* as saying that the visit to Russia "showed that relations between Ukraine and Russia are entering an economic, rather than a political stage."

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Hryhorii Nemyria, Deputy Prime Minister summed up the visit: "By any standards this was a fruitful visit. Important agreements on gas and nuclear energy were reached and relationships in key economic sectors

deepened. It makes sense that we mend fences and become good neighbours while we continue to integrate into Euro-Atlantic structures."



Government Scores Marks on Crisis Management

It would be a brave man indeed who would say that Ukraine is experiencing the green shoots of recovery. But maybe, just maybe, the worst is behind it.

There have been a number of indicators – such as the rise in industrial output up 8.3 percent in March over February, a reduction in salary arrears, stabilisation of the hryvnia and banking system – that point to signs of economic improvement.



Although it is too early to check Ukraine's economy out of intensive care, the government's medicine appears to be taking effect. This has been helped greatly by its renewed cooperation with the International Monetary Fund (IMF), which will almost certainly make a \$2.8 billion second tranche payment later this month. On the strength of this, a log jam is about to be cleared which will result in further financial support from the likes of the World Bank and European Bank for Reconstruction and Development.

Despite this, the IMF predicts that Ukraine's economy will contract 8 percent in 2009, with a meagre 1 percent GDP growth in 2010. According to Tim Ash, head of research for CEEMA for the Royal Bank of Scotland, "The upside is that the external financing gap is being closed quickly with the current account improving rapidly." Figures released late last month revealed a four-fold shrinkage in the current account deficit, year on year to \$882 million on the strength of falling imports. Indeed, a 0.5 percent GDP surplus is now forecast in 2009.

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This news comes at a time when the IMF predicts that 16 countries that share the euro will see their economies shrink by a bruising 4.2 percent this year.

With a steep GDP decline in Ukraine, there has been concern that an associated drop in state revenues will severely impact budget financing. Indeed, budget revenues were down 13 percent year on year over the first few months of 2009. Recognising this, the IMF is being flexible and is prepared to allow half of the second tranche to be used to plug this gap. In addition, it has been actively pushing Ukraine to secure World Bank funding to fill the budget financing gap. So it is to be hoped that there will be more stimulus loans such as the \$400 million credit from the World Bank (secured last December) for road repairs and construction.



In addition, some \$2.5 billion has been secured from the World Bank, European Bank for Reconstruction and Development and the European Investment Bank to support the government's bank recapitalisation programme. Some 17 foreign banks have pledged to recapitalise their subsidiaries this year and the Ukrainian authorities have moved to take seven domestically-owned banks into administration.



Firm Crisis Management

But the Ukrainian economy is not merely surviving on the largesse of international institutions. True, the government has worked hard to secure their trust. A vital part of this has been passing unpalatable anti-crisis measures to curb public spending to balance public finances. In short, proving that the government is a good bet, possessing both the acumen and political will to manage its way out of the financial and economic crisis.

The authorities have implemented a number of fiscal measures – many of which are unpopular and painful in a presidential election year – such as increasing the excise on alcohol, tobacco and diesel. These and other measures reduced the budget deficit by 2 percent of GDP.



▲ Anders Åslund of the Peterson Institute for International Economics.

The government's success in reducing the level of salary arrears in the public and private sector, by 32.5 percent and 26.5 percent respectively, since the beginning of April, underlines further its determination to normalise economic activity.

Securing the pledge of €2.5 billion from the EU to modernise Ukraine's gas transportation system was another coup, which came hot on the heels of a 10-year natural gas deal with Russia. The agreement removes intermediaries and establishes a transparent framework that bodes well for the future.

Anders Åslund, who was an economic adviser to the Ukrainian government from 1994 to 1997, and is a senior fellow at the Peterson Institute for International Economics, praised the government's efforts. In an article, entitled 'Ukraine Above the Rest in Crisis Management' (*Moscow Times*, 22 April), he wrote: "Ukraine has shown exemplary crisis management thanks to a few Ukrainian top officials – notably Prime Minister Yulia Tymoshenko – and a good job by the international financial institutions."

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Free Trade Talks Get Underway

On 21 April, negotiations on a broad-based Free Trade Agreement between the four European Free Trade States (Iceland, Liechtenstein, Norway and Switzerland) and Ukraine, got underway in Kyiv.

The free trade talks stem from last September's EU-Ukraine Summit in Paris. At that meeting Ukraine was offered a new agreement with the title of "Association Agreement," that would replace the Partnership and Co-operation Agreement (PCA). An integral element of the proposed agreement was to conclude a "deep and comprehensive" Free Trade Agreement, of which these talks are a vital step.



Deputy Prime Minister Hryhoriy Nemyria and Minister of Economy Bogdan Danylyshyn stressed the significance of launching free trade negotiations in the midst of the current global financial and economic crisis and referenced the need for a strong political will to avoid protectionist measures.

The initial discussions will focus on establishing a joint document which details the general framework for the negotiations, as well as the scope and principles of the future Free Trade Agreement between the partners. The talks will also cover trade in industrial and farm products and services, as well as issues on investment and intellectual property rights.

Ukrainian officials are hopeful that a new strategic deal could be inked during the term of the Swedish presidency of the EU, which begins in the autumn of this year.

EU officials have expressed cautious optimism. "If things do not slow down for political reasons, hopefully we will be done by the end of the year," said Benita Ferrero-Waldner, EU Commissioner for External Relations and European Neighbourhood Policy.

Will the Real Arseniy Yatseniuk Please Stand Up

The rapid rise in popularity of Arseniy Yatseniuk, who was removed as parliamentary speaker in November 2008 by an opposition vote assisted by presidential chief of staff Viktor Baloha, has caught many Ukrainian and eastern Europe analysts by surprise. Drawing on a desire for "change," the *Financial Times* and *Foreign Affairs* magazine have labelled – wrongly – Mr Yatseniuk a "Ukrainian Obama," referring to Senator Barack Obama who won the November 2008 US presidential election.



▲ Arseniy Yatseniuk, former parliamentary speaker and presidential candidate.

As the spotlight falls on the upcoming presidential election on 25 October, the Ukrainian media and political analysts have begun to scrape away the veneer that has so far protected Mr Yatseniuk. To be considered as a serious candidate, the former speaker needs to answer the following questions.

1. What is the source of funding for Mr Yatseniuk's campaign? The answer is far from clear. Ukraine's second wealthiest businessman, Viktor Pinchuk, has admitted to funding Mr Yatseniuk and there are strong

rumours that RosUkrEnergco-owner Dmytro Firtash has also offered his support. In a long expose of Ukraine's oligarchs, the *Kyiv Post* (16 April) wrote, "Experts say the favoured presidential candidate for Pinchuk and controversial gas tycoon Dmytro Firtash is Yatseniuk."

"Big business support Mr Yatseniuk is not out of any love of "change,"" *Zerkalo Nedeli* (21-28 April) commented – a pun on the name of his budding party Front for Change. It's worth noting that the then opposition candidate Viktor Yushchenko campaigned on the same slogan, "change," in 2004.

2. Is Front for Change a real party? Even for a newly established party, Front for Change appears ephemeral and lacks a support network throughout Ukraine. This caused the deputy head of the Bloc of Yulia Tymoshenko (BYuT) parliamentary faction, Andriy Kozhemiakyn, to say that BYuT does not see any "political force" standing behind Mr Yatseniuk and therefore there is "nobody" with whom to negotiate any pre-election deal.



3. Will Mr Yatseniuk become President Viktor Yushchenko's chosen successor in a bid to halt Yulia Tymoshenko's election victory? A Kyiv International Institute for Sociology poll cited by *Ukrayinska Pravda* (22 April) asked Ukrainians who President Yushchenko sees as his successor, to which 34 percent responded Mr Yatseniuk. Only 4.2 and 3.5 percent of Ukrainians see Viktor Yanukovych and Ms Tymoshenko respectfully as Mr Yushchenko's successors.

Former President Leonid Kuchma has warmly praised Mr Yatseniuk as has President Yushchenko. During the US presidential election, the US Saturday Night Live television show used comedians to depict President George Bush, Senator John McCain and Governor Sarah Palin. The actor playing McCain is seen to be extremely unhappy at receiving the actor Bush's endorsement because of the real Bush's low popularity of 20 percent. Now think of Ukraine, where the real President Yushchenko has only 3 percent support. His support and that of Mr Kuchma's represent a poisoned chalice for Mr Yatseniuk. So will he distance himself from them? Who knows?

4. What are Mr Yatseniuk's domestic and foreign policy priorities? This question cannot continue to be side-stepped. Put simply, Mr Yatseniuk's positions on domestic and foreign affairs remain unknown to Ukrainians. His growth in popularity has therefore taken place in an ideological vacuum.



and relations with Russia.

The Ukrainian media has now begun to ask why Mr Yatseniuk has risen in popularity when his policies remain unknown. To-date Mr Yatseniuk has been unwilling to outline his views on important issues, such as combating the global crisis, government policies, the Russian language, NATO, RosUkrEnergo, the Black Sea Fleet, Russia's invasion of Georgia,

A Ukrainian political analyst asked in *Ukrayinska Pravda* (22 April) why former Defence Minister Anatoliy Hrytsenko's popularity had not grown, even though he had outlined his policies for the presidential race. By comparison, Mr Yatseniuk has become more popular without unveiling his platform. Mr Hrytsenko has a platform and views that one can choose to agree or disagree with, whereas "Yatseniuk has nothing at the public level – neither this nor that." Mr Yatseniuk has experienced an increase in popularity without "declaring any kind of position on any of the key questions" facing Ukraine.

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A detailed analysis of the Yatseniuk phenomenon appeared in *Zerkalo Nedeli* (21-28 April) by seasoned analyst Oleksiy Mustafin. He commented that, "Nearly all experts are in agreement with the view that the former speaker should take no gratitude (for his rise in popularity); he simply was in the right place at the right time."

Ukrainian experts remain unclear as to what Mr Yatseniuk stands for? He is described as a "liberal" only because he has on a few occasions criticised the government's social programme. "Arseniy Yatseniuk has throughout his career not been remembered by his reforms and achievements but only by a few gestures," *Zerkalo Nedeli* (21-28 April) wrote.

Mr Yatseniuk's views on foreign policy are even more opaque. His allegedly pro-European orientation is based on assumptions, not on his statements or platform. The fact that he speaks English and reads the *Financial Times* gave some analysts the basis to claim he is "pro-European" or "pro-Western."



Russian journalists have repeatedly – but unsuccessfully – quizzed Mr Yatseniuk about his views on NATO or the fate of the Black Sea Fleet.

Case of Déjà vu?

Ukraine faces the danger of 2004 being repeated again. In the 2004 elections, Mr Yushchenko outlined a programme entitled 'Ten Steps Towards the People' and published 14 draft decrees that he promised to issue if elected president. The programme and draft decrees became the basis for the government's programme approved by parliament in February 2005.

The preamble to the programme states, "The government programme is based on, and develops the basis of, the programme of Ukrainian President Viktor Yushchenko's 'Ten Steps Towards the People' and is line with the constitution of Ukraine." Needless to say, these have remained largely on paper and become a sad indictment of Mr Yushchenko's presidency.

Will Mr Yatseniuk follow President Yushchenko's footsteps in being a chameleon, promising one thing and doing another or promising nothing and undertaking no "change?" Writing in *Zerkalo Nedeli* (21-28 April), Mr Mustafin says, "To move ahead the country needs a leader who can propose to his fellow countrymen a real strategic goal." But this requires a platform and an ideology which Mr Yatseniuk pertinently seems to lack.



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