



## Ukraine Rejects Gas Theft Claim and Calls on EU

Ukraine's state-owned gas company, Naftohaz Ukrainy, has denied Russian accusations that it is stealing gas. However, a presidential aide gave a stark warning on Saturday that gas supplies to Europe could be impacted in two weeks time unless the dispute is resolved. In the meantime, Yuriy Prodan, Ukraine's Minister for Energy, has led a delegation to EU states to explain Ukraine's position, while President Viktor Yushchenko and Prime Minister Yulia Tymoshenko have invited the European Union (EU) to mediate in the dispute with Gazprom.



▲ Playing the energy card. Gazprom switched off gas supplies to Ukraine last Thursday. The move has raised new questions over its suitability as a major supplier of gas to Europe.

The supply of natural gas from Russia to Ukraine was cut off at 0700 hours GMT on Thursday, 1 January, after talks collapsed over the alleged non-payment of a debt and failure to agree a gas price for 2009.

The central issues concern a demand by Gazprom to pay an alleged debt of \$2 billion. Naftohaz said that it had paid \$1.5 billion to the Swiss intermediary company, RosUkrEnergo, that supplies Central Asian gas to Ukraine. But Gazprom is insisting on a further payment

of \$500 million for alleged late payment fees, the validity of which Naftohaz disputes and has stated its willingness to take to a court of arbitration.

The other major bone of contention is the failure to agree a gas price for 2009 and the fees Ukraine wants to charge for transporting Russian gas to Europe. About 80 percent of Russian gas exported to Europe is transported through Ukraine's ageing gas pipeline network. Currently, Gazprom enjoys a cut-price transport fee which is three-times below the market rate. Gazprom pays Ukraine \$1.70 to transport 1,000 cubic meters of gas per 100 kilometres (62 miles) and has insisted on keeping the price unchanged. In a joint letter to Gazprom, Ukraine's president and premier pointed out that the current fee is inadequate to fund the maintenance of the pipeline network.

### No Contract, No Gas!

According to Gazprom's Chairman, Alexei Miller, "as far as gas to Ukraine is concerned we have no signed contract and so no legal basis to supply gas to them."

Gazprom offered Ukraine a 2009 gas price of \$250 per thousand cubic metres, which amounts to a 40 percent hike over the 2008 price of \$179.50 per thousand cubic metres. Ukraine rejected this figure, stating that \$201 would be more appropriate.

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Gazprom reduced its offer to \$235 per thousand cubic metres but has since dug in its heels, maintaining that Ukraine pay a market price of \$418. But the price of gas is set to fall. Its price is linked to, but lags behind, the price of oil which has dropped three-fold since the summer.

"Ukraine is open to negotiation not intimidation," said Hryhoriy Nemyria, Deputy Prime Minister responsible for European integration, "and will do its utmost to guarantee no disruption in supply to our European neighbours."

**"Ukraine is open to negotiation not intimidation."**

Hryhoriy Nemyria, Deputy Prime Minister. ▶



However, President Yushchenko's envoy on energy security, Bohdan Sokolovsky, warned that although Ukraine will continue to ship gas to Europe, disruptions may occur in "10 to 15 days" unless Ukraine's gas is pumped along with supplies to Europe. Maintaining pressure in the pipeline system is essential to continue deliveries.

### Gas is Not Being Stolen



Naftohaz officials strenuously rejected Russian claims that gas meant for Europe was being stolen. Valentyn Zemlianskyi, Naftohaz's press spokesperson, said, "We are removing gas for technical purposes, in order to ensure the transit of Russian exports." Once again, this to ensure Naftohaz maintains the correct pressure in the pipeline network.

On Saturday, a Naftohaz official confirmed that Russia had actually reduced the amount of gas being shipped to Europe through Ukraine's pipelines by 21 million cubic metres a day to 284.5 million cubic metres.

The European Commission is monitoring the dispute very closely with the Czech presidency saying it would call a crisis meeting of envoys in Brussels on Monday.

Despite a major lobbying exercise and PR campaign to explain its actions, Gazprom has once again drawn considerable flak from the international community over its willingness to resort quickly to strong-arm tactics.

Tammy Lynch, a Senior Fellow at Boston University's Institute for the Study of Conflict, Ideology and Policy, writing for the *Huffington Post*, said: "forcing Ukraine to negotiate under the distress of having its gas turned off is a tactic that smacks of blackmail and intimidation."

Naftohaz officials have estimated that Ukraine has about 90 days worth of gas stored to see it through the crisis.

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## 2009 Budget Passed

**Ukraine's parliament, the Verkhovna Rada, has passed the national budget for 2009. On 26 December, 226 lawmakers out of 353 registered in the 450-seat chamber voted for the state budget. The same day, President Viktor Yushchenko signed it into law. Yet the ink was hardly dry before the new legislation provoked controversy.**

The 2009 budget foresees a deficit of 2.9 percent of GDP, which contradicts the balanced budget demanded by the International Monetary Fund (IMF). Also, it forecasts economic growth



of 0.4 percent with inflation below 10 percent. Some analysts believe these assumptions are too optimistic and have branded it a "political budget," saying that the economy is more likely to contract by around 2 percent with inflation at 13-15 percent.



▲ Managing Director of the IMF, Dominique Strauss-Kahn.

Compliance with the IMF conditions is vital if Ukraine is to secure further tranches of the \$16.4 billion loan facility agreed with the IMF last October. Another condition is the cap on the amount that can be drawn from foreign reserves to prop up the hryvnia.

Prime Minister Yulia Tymoshenko and President Yushchenko moved swiftly to assuage

concerns over the deficit. On Tuesday, a letter signed by the pair and addressed to IMF Managing Director, Dominique Strauss-Kahn, acknowledged that the budget "does not fully reflect specific indicators set down in the programme backed by the IMF."

**"Let us assure you that we are going to take resolute steps to guarantee the implementation of the programme."**

The letter went on to say: "Let us assure you that we are going to take resolute steps to guarantee the implementation of the programme, including the adjustment of the budget indicators, including those related to the pension reform and the policies on the population incomes."

The president and premier indicated that they were working jointly on a plan aimed at stabilising the economy and ensuring compliance with IMF requirements ahead of the IMF mission's visit to Ukraine in January.

"We will do all that is necessary to meet the prescribed conditions of the loan facility," added Viktor Pynzenyk, Minister for Finance.



## Parliament Demands Dismissal of Stelmakh

Ukraine's parliament has again demanded that the Governor of the National Bank of Ukraine (NBU), Volodymyr Stelmakh, step down following accusations of incompetence and corruption. The parliamentary motion followed allegations last month that central bank officials staged the collapse of the currency, the hryvnia, to benefit businessmen linked to the president's staff.

At times during the past 30 days, the hryvnia appeared to go into virtual free fall. At one point it slumped to UAH 10 to the dollar before recovering to UAH 7.8 on Friday. This compares with only UAH 4.9 to the dollar in September. Rumours that commercial banks have been engaged in currency speculation have been rife for several months.



According to Prime Minister Yulia Tymoshenko, the central bank was providing monetary support to commercial banks involved in the currency speculation scheme. Some 18 banks have been under investigation.



▲ The National Bank of Ukraine.

So far, Nadra Bank is the only bank to be named and shamed in the scandal.

Ms Tymoshenko said that the NBU funnelled UAH 40 billion to various banks, with nearly one-fifth, UAH 7.1 billion, to Nadra. "So such special banks as Nadra, among others, are keeping almost one billion dollars, waiting for the time when the hryvnia collapses," said the premier.



The alleged scheme suggested that the banks planned to wait for the hryvnia to hit rock bottom before using their foreign currency to buy hryvnia. A strengthening of the currency was then planned. The premier, who has called for a full, frank and transparent enquiry into the scandal, has sent a report on the affair to the respected British investigative NGO, Global Witness.

### Damaging to the Country

The depreciation of the hryvnia has far reaching consequences for Ukraine's creaking economy, which, until the summer, had grown spectacularly on the back of foreign credit. Nearly every area of the economy is exposed. For example, imported natural gas is purchased in dollars but domestic sales are in hryvnia. A doubling of the price of gas, at a time when many citizens are struggling to repay mortgages and fearing for their jobs, is socially and politically unacceptable.

### President Resists Stelmakh's Dismissal



▲ A man under siege: the Governor of the National Bank of Ukraine, Volodymyr Stelmakh.

President Viktor Yushchenko has resisted previous calls to dismiss Mr Stelmakh. It is believed that he will simply ignore the motion from parliament which is nonbinding. In reply, Mr Yushchenko contends that the country needs the expertise of his long-standing colleague at this time of crisis.

Yet over recent months, the international financial community has been dumbfounded by the actions of the NBU. Flip-flop intervention policies fritted away billions of dollars in foreign reserves and did little to prevent the hryvnia's spectacular decline. This has led to accusations of incompetence. Last month, *Fitch Ratings* described the pace of depreciation as "astonishing."

At the time, Andriy Kovalchuk, in *Holos Ukrainy*, wrote that the NBU is doing what it pleases and that the Verkhovna Rada and government are merely observers, but have to bear all the responsibility for the bank's blunders.

**"The ineptitude of the central bank is a long-standing concern."**

A London-based emerging markets analyst told *Inform*, "The ineptitude of the central bank is a long-standing concern."



## Hryvnia Rebounds

Ms Tymoshenko's revelations concerning the alleged currency scandal sparked a flurry of activity in the NBU that resulted in the hryvnia recovering substantial ground. This began with an NBU auction of dollars, a rise in refinancing rates, and was helped by greater stability in the Russian rouble. On Friday, trading in the hryvnia was light ahead of the Eastern Orthodox Church Christmas. The premier has estimated the economically justified exchange rate for the currency to be UAH 6.0-6.5 to the dollar.



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## Regions Threat: Duplicitous and Empty

**The Opposition force of the Party of Regions (PoR) has ended its silence and is flexing its muscles as it seeks to capitalise from the economic turmoil impacting Ukraine's fragile economy. It is a move that is calculating and no doubt tied to the start of its presidential campaign.**



The party which has its heartland in the industrial Donbass has recently threatened to launch mass strikes in protest against the new enlarged democratic government – a coalition that has yet to get its feet firmly under the table. It claims that such strikes are directed at the deteriorating economic situation in Ukraine and the government's alleged inability to deal with it. Predictably, the party's leader, Viktor Yanukovich, called for Prime Minister Yulia Tymoshenko's removal without granting the government sufficient time to witness the positive impact of its anti-crisis policies.

Demanding the passage of *its* own anti-crisis programme and the adoption of the 2009 budget (finally passed on 26 December 2008), Mr Yanukovich has said that he will give the government 100 days before his party will "rise up the entire country" on a blue tide of protest.

But, PoR views on the crisis have proven to be "duplicitous and empty."

**Duplicitous** because the PoR did not vote in October in support of the anti-crisis package that was adopted as a required step to obtain the IMF stand-by loan of \$16.4 billion. The package was adopted by parliament through the combined votes of the three political forces that went on to establish the enlarged democratic coalition: the Bloc of Yulia Tymoshenko (BYuT), Volodymyr Lytvyn bloc and the Our Ukraine-People's Self Defence bloc.

Indeed, the PoR has shrunk from taking a constructive role during the economic downturn. It spurned an opportunity to establish a coalition of national unity last month, and proved it was ambivalent about the economic crisis by failing to pitch in its support and work on joint plans to alleviate the effects of the slump.

Whilst the coalition with BYuT was rejected for a number of reasons, it soon became clear that the PoR's priority was not fighting the crisis but to change the constitution to a full parliamentary republic.



▲ Viktor Yanukovich, leader of the Party of Regions.



Instead of supporting national unity, it resorted to demagoguery, claiming that only it had the leadership skills to chart a path out of the economic crisis. This is nothing new. In 2006-2007, when Ukraine's economy was growing strongly, the PoR established the oddly titled "Anti-Crisis" coalition. Once again, its clarion call was to save the nation from a crisis engineered by two Orange governments. In reality it was saying that it did not respect any other political force in Ukraine as legitimate, and that only *it* was capable of running the country. BYuT faction leader Ivan Kyrylenko said on Channel 5 television, "I have never seen how Regions have been satisfied when a coalition was not created without them."

## Speaker Rebukes Yanukovich's Party

Volodymyr Lytvyn, the new speaker of parliament described the PoR's protest plans as "immoral," reiterating the need for unity in the face of a national crisis. "We need to bring peace to every family," he argued. In addition, the Interior Ministry warned rally organisers of the legal consequences for calling for violent protest directed against people and buildings.



▲ Volodymyr Lytvyn. Chairman (speaker) of the Verkhovna Rada.

**Empty** because the protests led by the PoR have traditionally been paid for, rather than being spontaneous, and because they could *backfire*. During its seven year existence, the PoR has had an appalling record of organising protests.

During the Orange Revolution, the PoR failed miserably to organise a counter-revolution. Protestors, who were paid to travel to Kyiv, disgraced their party through their copious consumption of alcohol.

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Some even defected to the Orange side and many returned to Donetsk after a couple of days sightseeing in Kyiv.

Similarly, since the Orange Revolution, protests organised in Kyiv by the PoR have been branded by the Ukrainian media as "political tourism." Eastern Ukrainians have been herded into trains or buses, brought to Kyiv on pain of losing their jobs if they did not, and paid a per diem. Hardly the cause for a spontaneous, bottom-up civil society.

*Backfire* because, as BYuT faction leader Mr Kyrylenko pointed out, he would like to see alongside the ranks of protestors bussed into Kyiv, those paymaster billionaires who became wealthy during the Yanukovich-led "Anti-Crisis" government. "These lads banally made copious amounts of money. The people could ask of them: Where are these billions? Maybe you can share it out with us lads?"

Indeed, these same PoR oligarchs, who will be laying off workers early this year, may well be feeling the pinch from the slump in demand for steel and withdrawal of foreign credit facilities. But rest assured they will not suffer from the crisis. Their personal wealth is in US dollars and kept offshore. Perhaps the rank and file of the PoR would be better off protesting about that?

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