Statement by Jan Piercy
Date of Meeting: September 12, 2000

UKRAINE: Country Assistance Strategy

1. We welcome this discussion of the second Ukraine CAS. The CAS objective, supporting implementation of a broad-based poverty reduction strategy and attaining job-creating, sustainable growth, is appropriate, given Ukraine’s declining living standards, dismal growth performance, and poor reform record since independence. While real GDP growth has resumed recently and the new government has demonstrated some progress (e.g. better quality budget, first steps in public administration reform implementation, improved energy sector cash collections), pressure to revert to offsets, nonpayments, and unsustainable policies is strong, given on-going financial crunches.

Program Strategy

2. We agree with the two-legged strategy that the Bank proposes for Ukraine, as concrete results should serve as the basis for engagement/assistance going forward. Should Ukraine remain in the low case, the Bank’s proposal of limited sector-specific assistance and TA seems appropriate. Ukraine’s spotty track record for reform and portfolio performance suggests that it would be prudent to exercise caution in elevating Ukraine to base case.

3. Further, we understand the rationale for the cross-sectoral, Programmatic Adjustment Loan (PAL)-focused CAS base case given growing social inequality and on-going corruption, corporate governance, and nonpayments problems. We welcome the focus on results, rather than just policy actions. However, the triggers listed on page 27 are short on objectively quantifiable benchmarks and specificity. Can staff provide greater details—for example, how much of a reduction in budget arrears and energy payment debts would be required? PAL conditions—which are also required for moving to base case-- must be sufficiently concrete to identify specific achievements necessary while remaining flexible enough to reward meaningful progress on reforms.
Program Content

4. We commend the proposed program on poverty reduction, improving institutional capacity, and governance. Box 2 and paragraphs 11 and 12 describe how poverty is mitigated by artificial means, for instance by open and hidden subsidies (such as tolerating non-payment of housing rent and utilities). The CAS notes the political and social difficulties of removing these subsidies even though they are fiscally unsustainable. How does the CAS intend to address this problem?

5. Several key sectors which play an important role in Ukraine’s economy appear to us to merit more attention than reflected in this CAS:

- **Financial Sector**: The weakness of Ukraine’s financial sector remains a serious obstacle to sustainable economic growth. The current situation surrounding Bank Ukraina (in particular, the authorities’ desire to avoid liquidation and instead transform the bank into an agricultural lending institution) underscores the likely financial and fiscal costs associated with poor banking policies in Ukraine. Against the backdrop of Ukraine’s virtually nonexistent financial sector, we would have liked to see much more attention to the financial sector in this CAS – including TA and other support for the drafting and implementation of laws establishing the legal basis for the financial sector and for secured lending, training in the use of international accounting and audit standards, etc.

   Financial integrity issues such as money laundering and poor financial supervision can affect a country’s development if pervasive in the financial and governance systems. To guard against this, we urge that the Bank include in future financial sector projects and possibly in the PALs, efforts to address issues such as drafting and implementation of anti-money laundering legislation, regulations requiring customer identification by financial institutions and record-keeping, and reporting suspicious transactions.

- **Agriculture**: We are concerned that the CAS does not give sufficient emphasis to agriculture, commensurate with its role in Ukraine’s economy. Given the extent of government intervention in this sector, IFI engagement seems particularly necessary. For starters, we urge the Bank to work with the Ukrainian authorities to reverse Presidential Decree 832, reasserting government influence over the grain market through its use of price regulation and export restrictions. Until such controls are eliminated, any work in market development would be counterproductive.

   The Bank, with the IMF, has an appropriate role to play in minimizing the role of the state in the input/output business, reducing barter trade, and, with land reform, creating the conditions for the injection of new capital. Specifically, for collective farm liquidation to succeed over the near term, the Ukraine Government needs assistance creating the right enabling legislation (new land code) and developing a title registration system. We are encouraged by the CAS’s inclusion of a title registration/distributions project.
• **Energy**: There have been some important positive developments in this sector recently (e.g. cash collections have increased from less than 10 percent to 40-50 percent). But, going forward, the Bank seems to be satisfied restricting its energy sector technical assistance/policy advice to the forum of the Power Sector Task Force Committee. We are encouraged that the World Bank will play an active role in the Committee, and urge the Bank to continue a strong energy policy dialogue, even under a low case scenario. But given the history of nonpayments, corruption, and poor governance in this sector, more needs to be done if Ukraine moves into the base case, especially since the Ukraine Government is currently making gestures toward implementing Power Sector Task Force reform initiatives in the electricity sector. We urge the Bank to work with the authorities on this front, especially with privatization and the drafting of legislation supporting the independence of both the regulatory commission and the wholesale energy market. The Bank should consider additional support, such as for the transmission system, during the CAS timeframe if Ukraine's performance merits it.

In the gas sector, growing arrears and the continued use of offsets and barter, especially vis-à-vis Russia, underscore the importance of Bank engagement. We understand that Ukraine is currently negotiating a new gas agreement with Russia, which may facilitate greater transparency through market-based pricing. We urge the Bank to place more emphasis on the gas sector, as growing gas arrears and Ukraine’s siphoning-off of gas from Russia clearly are not sustainable going forward.

• **Environment**: As the CAS well describes, the country faces a myriad of serious environmental concerns. We urge the Bank to be receptive to any GOU requests for support on environmental protection beyond the program set forth.

• **Anti-corruption**: The CAS describes how the Ukraine Government plans to increase accountability and meritocracy, and improve the legal and judicial sector. It notes that Ukraine has requested the Bank’s help in making its anti-corruption initiative more effective. We welcome these developments, and want to know more about the Bank’s specific plans. Even under the low case, this merits priority.

• **Gender/Trafficking in Women**: The CAS notes that trafficking of young women has reached unprecedented levels, even by FSU standards. It describes the limited access to credit and disproportionate job cuts experienced by women, but offers no specific remedies and programs to reverse these inequities. The prominence given this issue in the Bank’s Gender Policy suggests that the Bank should take a more active role mitigating the factors underlying such trafficking than is reflected here, with only a study on the gender dimension of transition. This CAS should take a stronger stand on this troubling issue and include more specific programmatic elements to improve economic opportunities for women in Ukraine.

• **HIV/AIDS**: The plans to combat TB/HIV-AIDS, in coordination with USAID and other donors, are welcome. Can staff tell us whether the Ukraine Government’s planned expenditures on HIV/AIDS are intended to increase commensurately? What specific programs does the Bank plan to arrest the spread of HIV/AIDS? In view of the problems identified in trafficking in women, what are plans for public information programs and outreach to at-risk populations?
• **Trade:** The CAS notes that Ukraine seeks accelerated WTO accession. While we understand that staff has provided some advice on certification and on meeting the government procurement code requirements, it would be worthwhile to provide targeted technical assistance to assist Ukraine achieve its goal of accession.

**Instruments**

6. Should Ukraine reach base case, we see many potential risks to the PALS that would be the centerpiece of the Bank’s program. Ukraine’s limited capacity and poor reform track record suggest that conditionality should be very specific, and that successive PALs should be structured to militate against possible reform reversal. It is important that there be clarity, and that conditions be stringent but realistic.

7. We support the Bank’s use of a tracking mechanism that would provide the Ukrainian authorities and the Bank with a greater degree of assurance and transparency on the proper use of Fund resources. We look forward to more details on how the mechanism would work. We urge the Bank to ensure that its tracking of Bank funds is strong.

8. We commend plans for the updates of the PER, CFAA, and CPAR (Annex B4), as these diagnostics are fundamental building blocks to this proposed lending program.

**CAS Disclosure and Participation**

9. We welcome the Ukraine Government’s decision to make the CAS public following Board discussion. Such transparency is an important part of bringing all stakeholders into the development process. We also welcome the participation by civil society that has gone into preparation of this CAS.

10. It will be important to ensure that dialogue with civil society continues in preparations on major operations under this CAS. In any operations affecting employment, such consultations should include representatives of trade unions, and consultations with the ILO. We note that Ukraine’s labor laws and practice discriminate against independent unions in favor of those associated with the state, and the independents should also be included in consultations. Further, we suggest that the Bank engage the Ukrainian authorities in a policy dialogue to bring labor laws into compliance with ILO standards and grant full legal standing to all union organizations.

11. In closing, we urge the Ukrainian authorities to implement the reforms that they have discussed with the Bank and the Fund, which are key precursors to achieve sustainable growth.