



Political and Economic Crisis in Ukraine

Anders Åslund says the jailing of Yulia Tymoshenko is indicative of a range of bad political and economic decisions deepening Ukraine's isolation.

Edited transcript, recorded October 13, 2011. © Peterson Institute for International Economics.

Steve Weisman: Ukraine has stirred a crisis over the jailing of the opposition leader Yulia Tymoshenko. This is Steve Weisman at the Peterson Institute for International Economics with Anders Åslund, senior fellow, to assess the repercussions. First, the news reports suggest that her jailing might be temporary. What's your assessment?

Anders Åslund: Basically I don't believe this, because all the time we have heard rumors that things are not going to become as bad as it looks. And then things have become even worse than it looked. So this is a steady stream of information that has so far turned out to be disinformation.

Steve Weisman: Disinformation?

Anders Åslund: Yes.

Steve Weisman: People are trying to confuse the outside world?

Anders Åslund: Yes. And President [Viktor] Yanukovich was very much into this four weeks ago, in Yalta, when he met EU [European Union] Commissioner Štefan Füle and the Swedish Minister for Foreign Affairs Carl Bildt, and nothing of what is said then has turned out to be correct as yet.

Steve Weisman: It's created a crisis for Ukraine and caused it to be isolated politically, and jeopardized its growing economic relation with Europe. How concerned is the Ukrainian leadership?

Anders Åslund: I don't know if they are really concerned, because they seem to be pushing ahead brutally with what they want to do. But this is a very unwise line. And the question is how much they can really afford. Because what is happening now is that Ukraine is isolating itself from everybody. Russia –

Steve Weisman: Even Russia?

Anders Åslund: Most of all. The European Union, the United States. And it [Ukraine] has a terrible relationship with the IMF [International Monetary Fund]. And it's isolating itself from its population. Yanukovich's popularity rating is now down to fourteen percent.

Steve Weisman: He only narrowly won the election.

Anders Åslund: He did.

Steve Weisman: It's a little counterintuitive that Russia has joined the chorus of criticism. What's behind that?

Anders Åslund: For example, too many Russian-owned enterprises have been raided by General Yanukovich's oligarchs. You may say stolen by them, and Russia is not happy about that. And the personal relationship with Yanukovich and Putin, for various personal reasons, is atrociously bad.

Steve Weisman: Despite the suggestions that Yanukovich's party is more oriented toward good relations with Russia. How could that happen?

Anders Åslund: Russian enterprises are not allowed to buy Ukrainian enterprises today. Apart from capital purchases in the spring of 2010, nothing has been bought by Russians, public or private companies.

Steve Weisman: You've written about Ukraine's moves toward becoming a market economy. Is that in jeopardy, and are the economic repercussions of this latest action endangering Ukraine's economy?

Anders Åslund: Oh, sure. It is endangering the economy, not the market economy.

Steve Weisman: Right.

Anders Åslund: But what we are seeing is that the business environment, according to the European business association that makes quarterly surveys, has sharply deteriorated. And in particular we are seeing that the new tax code is used in various ways to close down about one hundred thousand small enterprises each month. So this is a devastation of small enterprises in favor of the big enterprises that are supported by Yanukovich.

Steve Weisman: The tax code, meaning the increased taxes on small businesses?

Anders Åslund: There are many things. The most important is that enterprises with regular taxation, which is very complicated in Ukraine, are not allowed to buy anything from enterprises that are not fully registered with the value-added tax. And a large sector of the Ukrainian economy has been relieved from the value-added tax. Basically, a small enterprise can't manage the normal tax system in Ukraine, because it's so onerous, [and] considered to be the very worst [in the world] by the World Bank.

Steve Weisman: What other steps is Ukraine taking that are adversely affecting its economy?

Anders Åslund: Ukraine has a fixed exchange rate to the dollar while the euro is falling. And there is a wide view that this is untenable. There was a capital flight in the month of September of \$3 billion. That is almost ten percent of currency reserves. And this is essentially ordinary people that are exchanging their [Ukrainian national currency] **hryvnia** savings for a dollar, because they don't think that the government is able to maintain the exchange rate.

Steve Weisman: Why is the government doing it?

Anders Åslund: Yes, it's a bad policy. If you have a commodity-based export, then you would like to have a floating exchange rate. And if you are a large economy, you will prefer to do inflation targeting. The IMF has ordered this for years, and the Ukrainian National Bank, which is not the most professional, simply refuses to follow the IMF advice.

Steve Weisman: Where are we headed with this? Can the Yanukovich government adjust its course?

Anders Åslund: So far it has not adjusted its course. It keeps up a budget reasonably through a vicious tax collection; in the first quarter of this year, tax revenues increased by forty percent in nominal terms. And growth is likely to be four percent or so this year, but it's very much dependent on steel and chemicals that account for half the exports. If those prices go down, the situation deteriorates. And basically, this is supporting the old obsolete sectors of the economy and killing off modern sectors of the economy, with the exception of agriculture, which is developing. So there are a number of broad expectations of devaluation, because the economic policy is simply so hostile, both to other countries and to the domestic small and medium size businessmen. And basically you can't continue this for a long time.

Steve Weisman: But they should devalue.

Anders Åslund: They should let the exchange rate float.

Steve Weisman: Right.

Anders Åslund: Rather than defend it fondly as they do today. And of course, they should deregulate the economy rather than killing off hundreds of thousands of small enterprises for no good reason whatsoever.

Steve Weisman: After alienating people who were very hopeful and supportive of Ukraine, do you see any prospect for the international pressure changing the situation in Kiev or in the country?

Anders Åslund: Something has to give. And it's difficult to see that there will be any popular uprising any time soon. I think that the scheduled parliamentary elections for October next year will be the point of change. And that politically, and economically, is simply a question of how much they can manage, because Ukraine has a large short term debt service, not so large a public debt altogether, but it's 45 percent of GDP – that's not small. And if you are not enjoying much confidence anywhere, then you can't refinance. So Ukraine may very well hit a wall of a sudden stop that nobody wants to refinance any longer. So for example, both domestic bonds and euro bonds are now closed for Ukraine. And then you should be scared.

Steve Weisman: Thank you, Anders.

