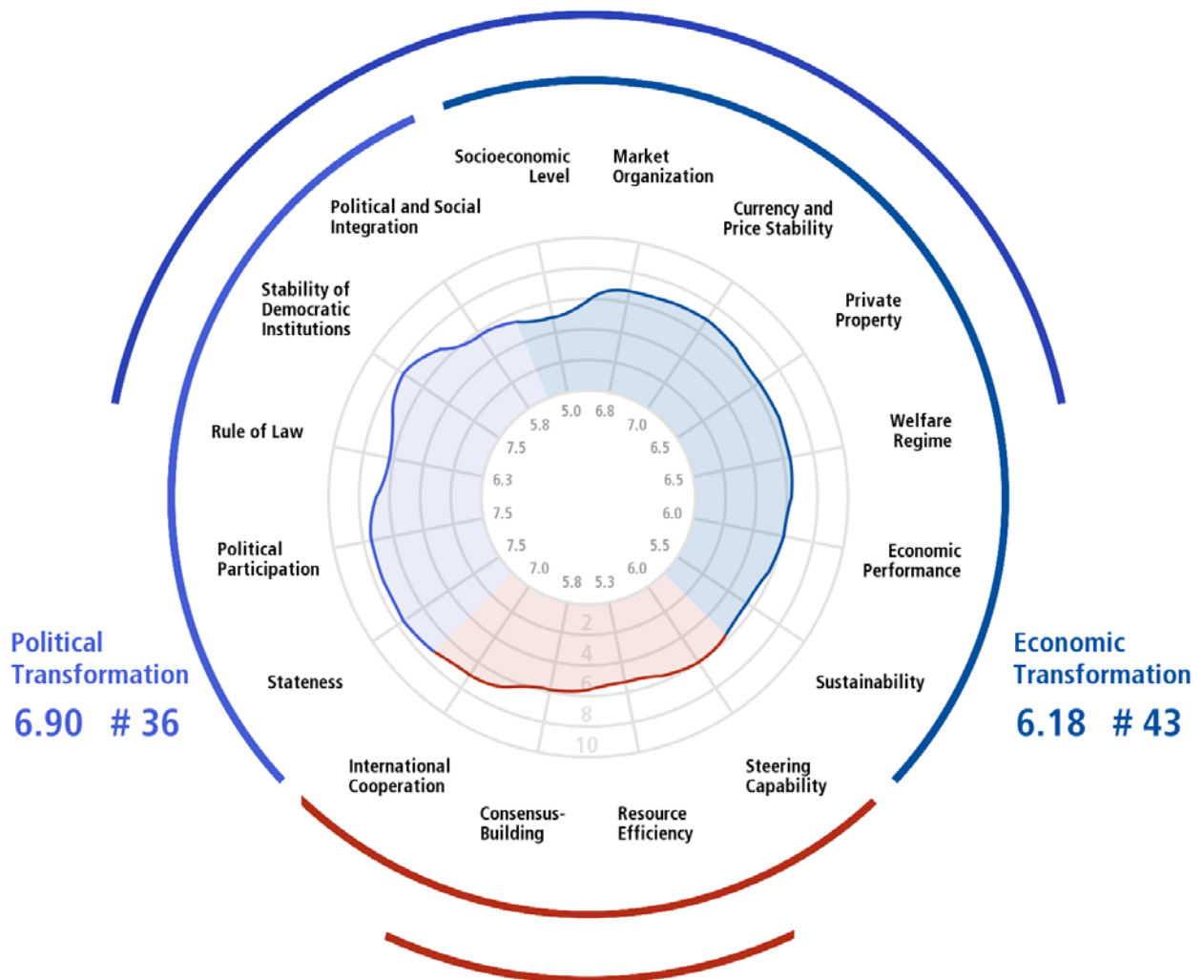


# Ukraine

## Status Index

**6.54 # 36**

on 1-10 scale out of 129



**Political Transformation**  
**6.90 # 36**

**Economic Transformation**  
**6.18 # 43**

## Governance Index

**5.41 # 49**

on 1-10 scale out of 129

This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2018. It covers the period from February 1, 2015 to January 31, 2017. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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## Key Indicators

Population	M	45.0	HDI	0.743	GDP p.c., PPP \$	8272
Pop. growth <sup>1</sup>	% p.a.	-0.3	HDI rank of 188	84	Gini Index	25.5
Life expectancy	years	71.2	UN Education Index	0.825	Poverty <sup>3</sup>	% 0.5
Urban population	%	69.9	Gender inequality <sup>2</sup>	0.284	Aid per capita \$	32.3

Sources (as of October 2017): The World Bank, World Development Indicators 2017 | UNDP, Human Development Report 2016. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

## Executive Summary

The period under review can be characterized by three major trends. First, Ukraine has been experiencing a painful struggle between the drivers of the reform process who want to overhaul the entire system of governance and the old system and structures that aim at preserving what can be named as “captured state.” The current political elites mostly represent the old system, but under the pressure of newcomers in the government and the parliament, civil society and international organizations have launched important reforms. Important and independent institutions to fight corruption were set up, a new patrol police force was established, state funding for political parties and transparency in media ownership were introduced, and reforms of the judiciary and civil service have been initiated, to mention just several areas of reform. This is an impressive set of reforms compared to all previous years since independence that took place under the combined pressure of civil society, international actors and enclaves of reformers among the political elites. At the same time, resistance from adherents to the old system has been strong and responsible for too slow a pace of change and the failure of some reforms. Oligarchs still exercise enormous political and economic influence, while conditions for the development of the middle class have not really improved.

Second, Ukraine has been coping with a disastrous economic situation. In 2016, after several years of recession, real GDP growth resumed thanks to an intensification in investments. Inflation declined, while the fiscal and external balances improved. The list of crucial economic reforms includes energy-sector reform, tax reform, public procurement reform, extensive deregulation, harmonization with EU norms, introduction of inflation targeting, fiscal decentralization and strengthened anti-raiding measures, among others. Many reforms are still ongoing, but these changes are the most significant since the country’s independence.

Third, Ukraine has been at war with Russia, having lost control over some 12% of its territory, through the annexation of Crimea and through the so-called and self-proclaimed Donetsk People’s Republic and Luhansk People’s Republic. Despite the Minsk process aimed at resolving the

conflict with participation from Germany and France, no cease-fire has been achieved, with numerous casualties, including among civilians, occurring almost daily. From April 2014 to December 2016, the war took the lives of 9,758 persons, while 22,779 were injured and over one million internally displaced. The war puts a heavy burden on Ukraine, both materially and emotionally.

In short, although Ukraine made important breakthroughs in its reform process, thanks to progressive pressures from inside, below and outside, the achievements so far are not sustainable and need to be defended every day. Although Ukraine managed to avoid early parliamentary elections in 2015 and 2016, populist parties and actors resisting reforms and taking advantage of the dissatisfaction of vulnerable groups among the population to stir up unrest are still a challenge. The war in Donbas and Russia's aggressive policies increase the difficulties, while the EU, although playing an important role in providing reform assistance, has not been able to respond adequately to the long-term challenge Russia presents. This might result in a weakening of the EU's transformative power in Ukraine, especially given the EU's own domestic turbulences.

## History and Characteristics of Transformation

Since Ukraine gained independence in 1991, its transformation has been largely determined by a narrow circle of elite groups. They shaped the new institutional framework according to their own particularistic interests. Amid sluggish reforms, influential industrial-economic groups and oligarchs emerged and a patron-client relationship between the president and these groups developed. This was reinforced by non-transparent large-scale privatization. Due to flawed procedures and favoritism, many large enterprises were sold far below market value and ended up in the hands of these groups, resulting in what can be called a "captured state."

From 1996 until 2005, Ukraine was formally a semi-presidential system. Leonid Kuchma's second term (1999–2004) was characterized by increasing authoritarian tendencies and informal power relations. Various protests against his regime galvanized opposition movements which finally led to the Orange Revolution. This occurred at the end of 2004, triggered by fraudulent presidential elections. The key demand of the protesters – free and fair elections – was realized. The inauguration of Viktor Yushchenko as president in January 2005 and the parliamentary approval of Yulia Tymoshenko as prime minister in February 2005 marked a significant shift in power. However, few expectations and promises (more democracy, transparency and socioeconomic change) were realized, and public disillusionment ensued. During the Orange period between the 2004 and the 2010 presidential elections, most of the Ukrainian government suffered from internal disunity and constant competition for power, facilitated by pervasive corruption and a lack of both expertise and checks and balances in the constitution that was amended in December 2004 (and took effect on January 1, 2006). The latter essentially established a parliamentary presidential system, reallocating power and competencies between president, government and parliament.

In February 2010, Viktor Yanukovich won the presidential election with a narrow margin against Yulia Tymoshenko, who became leader of the opposition. The years of the Yanukovich presidency saw the restoration of the authoritarian state. Yanukovich repealed the amendments to the constitution passed in 2004 and returned Ukraine to a semi-presidential system. Human rights as well as freedom of expression and assembly deteriorated. The opposition, harassed by a subservient judiciary, proved weak and unable to resist. When Yanukovich declined to sign the Association Agreement with the EU in November 2013, unexpected mass protests broke out and despite state violence that took lives of over 100 people, lasted through the end of February 2014, forcing Yanukovich to flee the country.

Until 2000, Ukraine's economy was in transformation recession. The first ten years of independence were marked by hyperinflation, high unemployment and falling standards of living. Between 2000 and 2008, Ukraine enjoyed a period of economic growth fueled by favorable external market conditions. Real GDP grew at about 7% on average. By 2005, the private sector's share of GDP reached about 60%. Poverty was reduced and disposable incomes increased. The financial sector crisis that hit Ukraine in 2008 revealed all the deficiencies of incomplete reforms, which were partly forgotten amid the economic growth of the preceding years. Although the economic situation stabilized in 2010, the country did not return to a path of stable growth. Ukraine continued to suffer from non-transparent clientelistic politics and structural imbalances. Yanukovich's economic policy and corruption exacerbated the situation even more, almost bringing the country to default.

Until 2014, when the Association Agreement with the EU was finally signed and ratified, Ukraine maintained a balanced foreign policy between Russia and the West. After the Orange Revolution in 2004, the Ukrainian government drew closer to NATO and the European Union, while relations with Russia deteriorated. However, Ukraine's hopes for becoming a candidate for EU membership and being admitted to the NATO Membership Action Plan did not materialize. Ukraine became a part of the European Neighborhood Policy and later the Eastern Partnership Initiative. Meanwhile, relations with Russia turned increasingly problematic. There were repeated trade conflicts, as well as conflicts over gas deliveries, transit and payments. Moreover, Russia attempted to block the signature of the Association Agreement between Ukraine and the EU and make Ukraine join its Eurasian Economic Union. Russia's military aggression and the annexation of Crimea in spring 2014 ended the balancing act. The post-Euromaidan authorities embarked on a clear pro-European course, backed by strong support for the EU and (to varying degrees) for NATO in Ukraine's public opinion.

Euromaidan protests, also known as the Revolution of Dignity, opened up an opportunity, which was missed ten years ago, after the Orange Revolution – an opportunity to dismantle the “captured” oligarchic-driven state and stick to the European course in terms of choice of social contract and international orientation.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

## Transformation Status

### I. Political Transformation

#### 1 | Stateness

The state does not hold a monopoly on the use of force throughout the territory of Ukraine. Twelve percent of Ukrainian territory (47 thousand square kilometers) is occupied by foreign administrations or forces. This includes Crimea, which was annexed by Russia in March 2014, and parts of the territory of Luhansk and Donetsk regions, where the so-called and self-proclaimed Luhansk People's Republic (LNR) and Donetsk People's Republic (DNR) were established in May 2014.

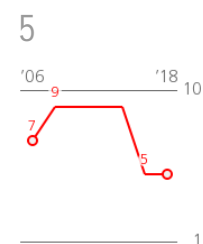
Despite numerous attempts to establish a cease-fire, the war between the rebel-controlled Donetsk and Luhansk regions (with Russia behind them) and the Ukrainian state still continues. With regards to the territory under the control of the Ukrainian state, initially, in early 2014, a number of volunteer battalions were established and it took time until they became completely subordinated to the central command of the so-called Anti-Terrorist Operation led by the Ukrainian Security Service. However, a lot of illegal weapons are circulating in Ukraine. According to the media, since the war broke out in early 2014, the number of illegal weapons grew from 3-3.5 million units to 4.5-5 million units and this trend continues. In the medium and longer term, this may endanger the state's monopoly on the use of force.

The Ukrainian nation-state is accepted by all relevant actors and groups in Ukraine, apart from Crimea and the temporarily occupied territories in Donbas. It should also be noted that before the Russian intervention, which started in 2014, there was no relevant challenge to the integrity of the Ukrainian state. Crimean separatism vanished a decade ago and separatism never was an issue for more than a handful of lone activists in pre-2014 Eastern Ukraine.

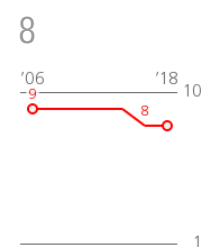
On the territory controlled by the Ukrainian state, identification with the Ukrainian state has been growing in recent years. However, for a considerable part of the population, acceptance of the Ukrainian nation-state is still more an issue of pragmatism than of deep conviction. In opinion polls from 2014/15, a third of the

Question  
Score

Monopoly on the  
use of force



State identity



population still claims to regret the dissolution of the Soviet Union (down from nearly half in 2010). Opinion polls conducted after Euromaidan also showed that identification with the Ukrainian state, as compared to other identifications (for instance, local or regional), grew significantly. According to a poll conducted by the Razumkov Center, 58% of citizens identify themselves primarily as Ukrainian citizens, while local and regional identities are less pronounced – 22% and 11% respectively. Of those polled 67% consider themselves to be the patriots of Ukraine.

The only large ethnic minority in Ukraine are Russians. The 2001 census (the most recent one) had already revealed that 77.8% of people self-identified as Ukrainian, while 17.3% self-identified as Russian. At the same time, 67.5% identified Ukrainian as their mother tongue, while 29.6% identified Russian as their mother tongue.

All citizens enjoy the same civil rights. In 1991, every person residing in Ukraine became entitled to Ukrainian citizenship, regardless of nationality. Ukraine thus emerged as a civic nation, and the nation-state's legitimacy is accepted by all relevant groups. Ukraine does not recognize dual citizenship, but the law on citizenship does not punish it. As a result, there are cases of acquisition of Russian, Romanian and Hungarian citizenship by Ukrainians, especially in western Ukraine and Crimea. Many (elderly) members of the Roma minority do not have Ukrainian passports.

Church and state are separated and the political process is secularized. The heterogeneous religious landscape, combined with the secular Soviet past, prevents the impact of religious dogmas on state policy. According to a poll conducted by the Kyiv International Institute of Sociology in May 2016, 80% of respondents considered themselves to be Christian and 12% said that they do not belong to any religion, but are believers.

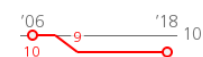
There are five major churches: the Ukrainian Orthodox Church (Moscow Patriarchate), the Ukrainian Orthodox Church (Kiev Patriarchate), the Ukrainian Autocephalous Orthodox Church, and two Catholic churches (Greek and Roman Catholic). None of them functions as a state church. In addition, there are Jewish and Muslim communities and a growing number of Protestant and Evangelical groups.

The Ukrainian Orthodox Church (Moscow Patriarchate) has the largest number of parishes, while the Ukrainian Orthodox Church (Kiev Patriarchate) has the largest number of adherents and this number grew at the expense of the Moscow Patriarchate church as reaction to the Russian military aggression. The Ukrainian Greek Catholic Church is the third largest and dominates in the west of Ukraine. Other churches have respective shares of less than 3% of the population.

There are no conflicts between the churches and the state. During election campaigns, political parties and individual politicians sometimes use the support of certain religious organizations. In June 2016, there was a situation in which politics and religion became intertwined. The parliament of Ukraine adopted an appeal to the

No interference of religious dogmas

9



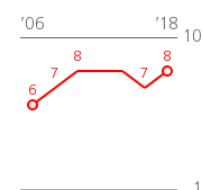
1

Patriarch of Constantinople Bartholomew with a call to issue a Tomos (decree of the head of the Church) regarding the autocephaly of the Orthodox Church in the country, which would overcome the division among the Orthodox Churches in Ukraine. As the reaction to this, the Ukrainian Orthodox Church of Moscow Patriarchate organized large religious processions throughout Ukraine. These were openly supported by the Opposition Bloc Party, while many politicians from the ruling coalition named the procession “a project of the Kremlin.”

Public administration functions on all administrative levels (with the exception of Crimea and the separatist-controlled areas of Donbas), albeit with varying degrees of effectiveness and state capture by economic actors. The low degree of decentralization also hampers more effective administration. However, since 2014 important institutional foundations to improve public administration were laid and have already affected the provision of services. Increased local budgets because of fiscal decentralization, the one-window policy for administrative services, increased access to and transparency of public information and the development of e-governance give citizens opportunities to make better use of public resources. With regard to public infrastructure, 98% of the population has access to running water and 95% has adequate access to improved sanitation facilities.

Basic  
administration

8

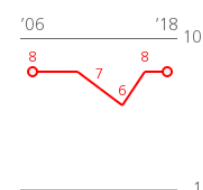


## 2 | Political Participation

The distribution of political offices takes place through general elections, which are conducted regularly, where universal suffrage with secret ballot is ensured and several parties with different platforms are able to run. During the period under assessment, no national (parliamentary or presidential) elections took place, although early parliamentary elections were discussed intensively as an option in political circles and the media.

Free and fair  
elections

8



In October and November (second round) 2015, local elections took place all over Ukraine (apart from the temporarily occupied territories, including Crimea). More than 350,000 candidates (representing 132 political parties and themselves as independents) were eligible for 168,450 positions as mayors of cities, villages and settlements and as deputies of local councils and for 1,600 regional council seats in 22 regional parliaments. While the OSCE and other international and domestic observers recognized that the elections were “competitive, well organized overall and the campaign generally showed respect for the democratic process,” they also noted the complexity of the legal framework, lack of confidence in the election administration and the dominance of powerful economic groups over the electoral process as big problems. Indeed, the relative success of several political projects with “oligarch” backing, such as Revival and the Ukrainian Association of Patriots (UKROP, supported by Ihor Kolomoisky) or the Opposition Bloc (Rinat Akhmetov and Serhiy Liovochkin) in some local elections provides an example of how financial



resources translated into political power. Domestic observers also noted another problem – namely, hidden vote buying, whereby various candidates engaged in charitable activities before elections to gain the sympathy of voters.

Election legislation for local elections was reformed in July 2015. The new law increased the election threshold from 3% to 5% and introduced three electoral systems for these local elections with the view to introduce new legislation before the next elections to take the results of decentralization reforms into account. There is a need for comprehensive electoral reform, including for parliamentary elections, to tackle numerous deficiencies that became evident during campaigning and voting. Despite the constant pressure from civil society and international observers, by the end of 2016, such reform was not yet on the agenda of decision-makers.

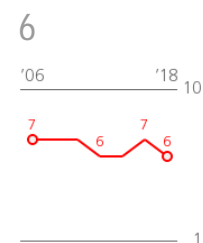
Elected rulers have the power to govern. The ruling coalition that emerged at the end of 2014 and had the constitutional majority was shaken by a political crisis in February to March 2016, caused by the resignation of the reformist Minister of Economy Aivaras Abromavičius in Arseniy Yatseniuk’s government. The coalition managed to survive with only the two biggest coalition partners staying in the coalition and the appointment of a new government headed by Volodymyr Groysman in April 2016.

However, the government is now even more dependent on support from other parliamentary groups, including those influenced by vested economic interests. The president has managed to bargain with representatives of these interests and offer them benefits, often at the expense of public good, so as to secure votes and relative stability. Some analysts call the arrangement “the social contract of corruption consensus.” The regular conflicts and scandals related to, for example, the attempts by oligarch Kolomoisky to maintain influence over majority state-owned companies and his ability to delay important legislation in parliament, demonstrate the political impact of vested economic interests, which do not amount to a veto power in the strict sense, but to power to delay and ensure a measure of bargaining. Another example is that of high electricity prices for the population resulting from the monopolistic position of the oligarch Akhmetov in the market supplying coal for electricity production.

At the same time, several anti-corruption initiatives promoted by civil society and foreign creditors aim to reduce the scope in which vested economic interests can influence policy-making.

Freedoms of association and assembly are guaranteed in the constitution and have been widely respected since the transition of power after the Revolution of Dignity in 2014. Since then numerous peaceful gatherings took place throughout Ukraine either in support of the territorial integrity of Ukraine or in support of separatist activities (the latter in smaller numbers). Peaceful gatherings organized by civil society activists near public buildings to advocate certain laws and decisions have

Effective power to govern



1

Association / assembly rights

9

taken place on many occasions and civil society organizations have faced no restrictions in their activities. By the same token, numerous protests against hikes in tariffs for municipal services, organized by oppositional parties and social groups, have taken place.

An important test was the Equality March to advocate for LGBTQ rights organized in June 2016 in Kiev. Police in large numbers protected the march against aggressive groups who tried to block it. Numerous civil society initiatives, registered and non-registered, enjoy the right to engage in activities and mobilize citizens.

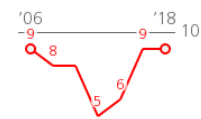
Freedom of expression and the prohibition of censorship in Ukraine are guaranteed by the constitution and a number of laws. Since the transition of power after the Revolution of Dignity, these have largely been respected; moreover, a number of reforms have been introduced to improve the situation.

As of April 2015, public broadcasting on national TV Channel 1 began. The reform is still under way and lacks state funding, but offers impartial content, supervised by an independent team of experts.

In October 2015, the Law on Transparency of Media Ownership came into force. According to the law, media had to disclose their ownership by the end of March 2016, which revealed large economic players (oligarchs) behind most media outlets.

Due to several laws adopted in 2015 and 2016, journalists acquired more opportunities to access information (for instance, recording court proceedings) and better protection under criminal law. All these reforms enhanced the access of Ukrainian citizens to a variety and plurality of both print and electronic media. The number of users of the internet, which offers a lot of independent civil society content, grew rapidly, to 65% in February 2016, up 8% compared to February 2014.

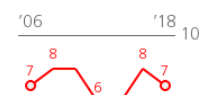
According to experts, freedom of expression in Ukraine has been hindered by de-communitization legislation, by legislation that bans or restricts content from the Russian Federation or which positively portrays the aggressor, security service actions against persons who are suspected to be linked to Russia's actions in Ukraine and even those who criticize military mobilization in Ukraine, and procedures for journalists to report from the regions occupied by Russia-controlled separatists. Moreover, several journalists have been victims of violent attacks, and some have been murdered.



1

Freedom of expression

7



1

### 3 | Rule of Law

The Ukrainian constitution provides for the separation of powers. Yet, the functions within the executive (between the president and the government) are not clearly delineated, giving too much space for informal arrangements. After the Orange Revolution this institutional framework paved the way for political infighting between the president and the prime minister. Since Euromaidan, luckily, this has not been the case. President Poroshenko managed to cooperate constructively with both prime ministers since then – Arseniy Yatseniuk and Dmytro Groysman.

Groysman, appointed in April 2016, is believed to be not really independent of Poroshenko, who is seen as trying to concentrate too much power in his own hands. The parliament has by and large demonstrated that it is able to put a check on the government, but since the ruling coalition needs votes from members of parliament from other factions and groups, many dominated by particularistic economic interests, the role of the president in helping to secure those votes is crucial.

Political independence of the judiciary and law enforcement has not yet been achieved, largely due to the highly volatile political situation in the country and the lack of a tradition of rule of law. The reform of the judiciary that was launched in 2016 might rectify these shortcomings in the long run.

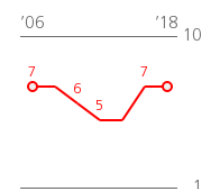
The judiciary in Ukraine has been one of the most corrupt and politically dependent state institutions with the lowest level of trust in society. Hence establishing an independent judiciary was recognized as one of the key reform areas after the Revolution of Dignity. Despite considerable pressure from civil society, foreign governments and the donor community, real reform did not start before 2016 when, in June 2016, the law that amended the constitution of Ukraine on the issues of judiciary and the law, On the Judicial System and the Status of Judges, implementing the new constitutional law, were passed. This legislation sets higher standards for judicial independence and ensures greater transparency of and public accountability among judges. It paves the way for reform of the prosecutor's office, and shapes the conditions for renewing the judicial system, including the establishment of a new Supreme Court with a fully updated panel of judges selected through a competitive appointment process.

As a result of the constitutional amendments and the introduction of a very comprehensive e-declaration system, around 1,000 judges resigned voluntarily, freeing space for a substantial renewal of the judiciary. The High Qualification Commission of Judges announced a competition for the new Supreme Court in November 2016.

As of January 2017, the law that paves the way for an overhaul of the Higher Council of Justice came into force. The renewed council will be an independent body that will

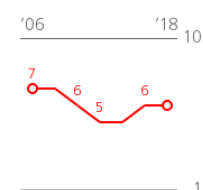
Separation of powers

7



Independent judiciary

6



have the powers to suggest candidates for judges to be appointed by the president, dismiss judges and make decisions in response to violations by judges. Although all these initiatives are a real breakthrough for judicial reform, implementation that will bring about change is still to follow.

Political corruption is still widespread in Ukraine, but thus far, there have been barely any cases where anyone has been brought to justice. A number of anti-corruption initiatives, among them the establishment of the Anti-Corruption Bureau, were launched after Euromaidan. The bureau is independent and operates professionally. Between December 2015, when it began work, and September 2016, it launched 245 investigations and passed 31 cases on to the courts; but due to an unreformed judiciary these cases were not pursued.

The Prosecutor's Office launched cases against several officials from the times of Viktor Yanukovich's presidency and Prosecutor General Yuri Lutsenko announced that in 2016 that several big cases would be investigated, including against officials currently in office. However, no such cases ended up in court. A few prominent detentions include those of members of parliament Ihor Mosiychuk of the Radical Party and Hennadiy Korban of the UKROP party. In other cases, such as that of member of parliament Mykola Martynenko (a close ally of former Prime Minister Arseniy Yatseniuk) and former Prosecutor General, Viktor Shokin (a personal friend of President Poroshenko), the suspects had to give up their posts after tremendous pressure was exerted, including from the West.

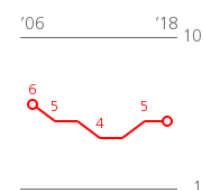
Quite a few officials and judges resigned voluntarily due to the introduction of a very comprehensive e-declaration system in 2016. Yet many other individuals from the former Party of Regions or allies of President Poroshenko and current officials, subject to corruption investigations, remain in political office.

Respect for civil rights has considerably improved following the transition of power in February 2014. The government reduced the level of interference by tax and other authorities in business operations. In addition, the powers of the prosecutor's office to engage in general supervision have been revoked. These powers allowed for the carrying out of inspections of any business, thus significantly increasing prosecutors' punitive clout and opportunities for corruption.

However, it is still difficult for an individual to protect his/her rights in the courts of general jurisdiction if those are violated by an unconstitutional act of the president or the government, as individuals do not have the right to apply to the Constitutional Court directly in these cases. But as part of the reform of the prosecutor's office, 100 free legal aid centers were opened in July 2015. These provide low-income individuals with free legal advice, as well as ensure legal representation of such persons in civil and administrative cases. In September 2016, an additional 402 legal aid bureaus were established with the aim of providing the same categories of people with legal advice and consultations, but without legal representation. These legal aid

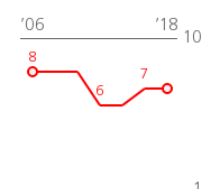
#### Prosecution of office abuse

5



#### Civil rights

7



centers and bureaus can have an enormous impact on nearly eight million potential clients.

Freedom of movement and freedom of religion are, by and large, ensured and there is no noteworthy ethnic discrimination. The current legislation includes under discrimination, inter alia, age, skin color, physical condition (disabilities), family status and sexual orientation. Although these rights cannot be enforced in all cases, the police were able to protect the Equality March organized in June 2016 from assaults by aggressive groups that tried to block it.

The situation in the conflict zone in Eastern Ukraine is different. Human rights organizations have repeatedly documented larger numbers of cases where volunteer battalions' representatives in the territory controlled by the state of Ukraine ignored individuals' right to life and security, the prohibition on torture, and engaged in cruel and inhuman treatment.

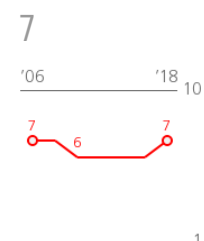
#### 4 | Stability of Democratic Institutions

Soon after the Euromaidan protests, major democratic institutions were reestablished. Ukraine returned to the constitutional provisions that ensure power-sharing between the president and the parliament/cabinet. Early presidential and parliamentary elections that took place in 2014 in a free and fair manner were followed by local elections in 2015.

However, the effectiveness of these institutions is partially impaired as a result of the legacy of previous regimes. The judiciary, the civil service, the Office of the General Prosecutor and other institutions are still dominated by people who represent the old system and particularistic networks. Apart from these legacies, a number of other factors still hamper the functioning of democratic institutions. These include poor delineation of powers between the president and the prime minister, poor delineation of powers between the representatives of the executive vertical and elected authorities at the local level, and inefficiency in the civil service, law-enforcement authorities and judiciary. These problems are being tackled by some reform initiatives. In 2015, a new patrol police force equipped with newly selected and trained personnel appeared all over Ukraine. Initial steps in the renewal of the corps of judges and civil servants were made, but it is too early to talk about success.

All influential political actors formally accept democratic institutions – at least in rhetoric and in political programs. No political force claims that democracy is alien to Ukraine or that it has been imposed from outside. However, in practice there is a temptation to misuse and abuse political power and therefore to undermine democratic principles.

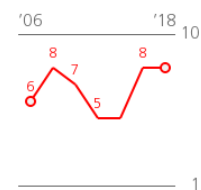
Performance of democratic institutions



Commitment to democratic institutions

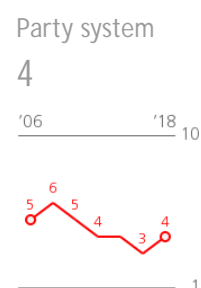
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The political culture in Ukraine is not mature enough and democratic institutions are very fragile. Many political actors seem unaware of some of the basic ideas of a democratic system, such as respect for opponents' views and there are many examples of undemocratic behavior within democratic institutions. Moreover, some democratic institutions are not accepted as legitimate on the basis of accusations that they are prone to corruption and politically dependent, such as parts of judiciary, law enforcement and civil service. Associations, civic organizations and the military work within democratic norms, while some interest groups, such as oligarchs, still prefer informal networks to promote their interests.



## 5 | Political and Social Integration

The party system in Ukraine is very unstable and volatile. There are numerous political projects, rather than parties, that appear and disappear depending on circumstances. They have no clear programmatic differences and continue to be primarily political vehicles for particularistic interests of leading politicians or businesses, rather than aggregating and representing societal interests. On the whole, the battle lines between parties are blurred and change frequently, driven by power interests rather than ideology or party programs. For instance, most political parties that passed the 5% threshold in the 2014 parliamentary elections were newly registered, although they comprised the same old politicians. At the local level, parties with strong oligarchic financial backing, such as the Opposition Bloc or UKROP succeeded in several regions and local communities.



The fragmentation of the party system is low. Only a small number of parties get into parliament, although many more run in elections (52 political parties competed in the October 2014 parliamentary elections, but only six won seats; in the local elections of 2015 candidates representing 132 parties competed).

An important trend with potential long-term implications is that of the emergence of new political parties that compete for the electorate with values of democratic modernization (the part of the electorate that was active in or supported the Maidan protests). Analysts estimate that 15–20% of the electorate would vote for these parties. At the moment, three such parties can be named. One is the People's Power Party, which won 230 seats in 62 local councils and mayoral positions in twenty regions of Ukraine in local elections in 2015. This party had only 200 members in 2014. By the 2015 local elections, membership had increased to almost 3,000. Two other parties that were announced later in 2016 are the Democratic Alliance Party and the Movement of New Forces Party. The first includes many members of parliament who entered parliament as members of old parties, but represent new values. The second is headed by the former president of Georgia and former governor of Odessa Region, Mikhail Saakashvili. Laws on transparency in media ownership and demanding that all parties disclose their sources of funding (envisaging state funding

to political parties) were passed in autumn 2015 and will help these parties to succeed in the long run. Yet, for the upcoming elections the three parties will have to unite to avoid competing for the same electorate.

To sum up, it can be stated that the Ukrainian party system is in constant flux and that no party has deep roots in society. New legislation on political parties may promote a consolidation of the party system in the long run, but immediate changes are not to be expected.

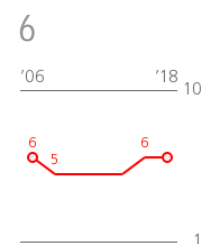
At the national level, the formal channels for communicating societal or group interests are not well defined. The network of interest groups is relatively close-knit, but their influence is very unequal. Civil society has managed to increase its presence in public discourse and policy-making by forming platforms and coalitions. One of the most prominent examples is the Reanimation Package of Reforms, launched after the Euromaidan protests, a platform that brings together over 70 NGOs and 23 expert groups on various issues. The platform succeeded in promoting a number of important reforms by combining expertise with targeted advocacy. Civil society in Ukraine has become a real driving force behind the reform process.

Financial and industrial groups or oligarchs are well represented in decision-making, although mostly through non-transparent channels. Such groups as System Capital Management (Rinat Akhmetov), Private (Ihor Kolomoisky) and Interpipe (Viktor Pinchuk), to mention a few, own popular media, finance political parties or influence the government through informal channels and thus ensure that their interests are represented in decision-making at the national and local level.

Other societal interests are less well represented. Ethnic, nationalist and religious mobilization has not played a role in the formation of interest groups in Ukraine. One exception could be Crimean Tatars who, after the annexation of Crimea, have doubled their efforts to influence the policies of Ukraine toward Crimean Tatars, many of whom moved to mainland Ukraine, as well as Kiev's policy towards annexed Crimea.

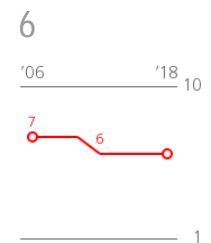
Despite relatively high (formal) membership in trade unions, these have played a marginal role in promoting issues important for employees, such as workplace safety or better social conditions. Consumers in Ukraine, although potentially the largest interest group, have not been sufficiently organized to influence policy. Business associations, in view of the Association Agreement with the EU, have begun to represent their interests to the government. However, the influence of such groups has remained weak, not the least due to their low capacity to set agendas and articulate their interests.

Interest groups



The people of Ukraine generally endorse democratic norms. In a poll conducted by the Democratic Initiatives Foundation in July 2016, 54% of the population agreed that democracy is the best system of governance for Ukraine; 20% supported an authoritarian regime; while 15% were indifferent. Sometimes, as surveys show, social and security sector reforms are greater priorities than democracy. This can be explained by the significant deterioration of the economic situation, currency devaluation and the war in Donbas. In a poll conducted in December 2016 by the Democratic Initiatives Foundation and the Razumkov Center, people mentioned that the authorities should focus on stabilizing the situation/achieving peace in Donbas (75%), reducing tariffs and prices (56%), stimulating economic growth and creating favorable conditions for business (48%), fighting corruption (46%) and increasing salaries and pensions (42%). Interestingly, a significant number of people are ready to tolerate material difficulties for the sake of the success of reforms (35%), although the percentage of people who are not ready to do so is 55%. This is against the background of 73% of the population thinking that the situation in the country has been worsening (in both 2015 and 2016).

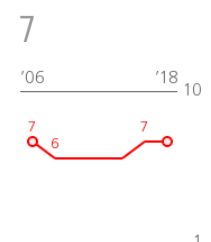
Approval of democracy



The public's trust in public institutions remains low. Only volunteer organizations, civil society organizations, the church, the army, volunteer battalions, the border management service, patrol police and Ukrainian mass media are more trusted than mistrusted. Not a single politician in Ukraine though enjoys more trust than mistrust. The state apparatus, courts, commercial banks, the National Bank of Ukraine (NBU), parliament, prosecutors and political parties enjoy the highest level of mistrust. The level of mistrust in the government, the president and other institutions is also high.

The growth of social capital in Ukraine has been remarkable, a trend that has its roots in the Euromaidan protests, where civil society organizations, voluntary initiatives and ordinary people played a decisive role (in contrast to political parties). Since Euromaidan, in the face of Russian aggression, people were eager to donate to the army and voluntary initiatives providing support to the army, volunteer battalions and the civilian population impacted by the war. All public opinion polls since Euromaidan have recorded the highest trust in voluntary initiatives, compared to other institutions (state and private) among the people. The poll in December 2016 by the Democratic Initiatives Foundation showed that the trust in voluntary initiatives exceeded mistrust by 44%. Indeed, the voluntary initiatives in Ukraine have mushroomed with more and more people being involved in different capacities.

Social capital



The level of trust in NGOs has also increased, with the level of trust exceeding the level of mistrust for the first time in December 2014 since Ukraine's independence. In total, there were almost 76,000 registered NGOs in Ukraine by the end of 2016 (representing an increase of over 20,000 since 2008). However, some estimates claim that only about 10% of these are active.



## II. Economic Transformation

### 6 | Level of Socioeconomic Development

In 2015, poverty in Ukraine remained elevated due to economic hardships and military aggression that caused significant internal migration. According to the World Bank, the poverty rate (under \$5/day in 2005 PPP) increased from 3.3% in 2014 to 5.8% in 2015, while moderate poverty (World Bank national methodology for Ukraine) grew from 15.2% in 2014 to 22.2% in 2015. In 2016, the level of poverty was somewhat reduced amid the improvement of the general economic situation. Real disposable household income increased by 7.3% year-on-year in the third quarter of 2016, marking the second quarter of positive growth rates after two years of decline.

In 2015 to 2016, the establishment of a business-enabling environment and promotion of small and medium business has been among public policy priorities to ensure inclusive economic development.

Ukraine is ranked 81st out of 187 countries in the Human Development Index (HDI) for 2014. It belongs to a group of high human development countries with a 0.747. The inequality-adjusted HDI places Ukraine 16 ranks higher than the standard HDI for 2014. According to the WB, the Gini coefficient for Ukraine is 24.1, which is at the level of developed countries.

Gender inequality is moderate. In the Gender Inequality Index for 2014, Ukraine is ranked 57th out of 154 countries with a 0.286 score, improving compared to previous years. Females have equal access to education, social security and the labor market, but tend to receive lower wages and are severely underrepresented in political life in the country.

There are no specific social barriers associated with religion, but social exclusion is registered for some ethnic minorities like Roma. Also, disabled people and people with HIV/AIDS continue to experience social exclusion.

Question  
Score

Socioeconomic  
barriers

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Economic indicators		2013	2014	2015	2016
GDP	\$ M	183310.1	133503.4	91031.0	<b>93270.5</b>
GDP growth	%	0.0	-6.6	-9.8	<b>2.3</b>
Inflation (CPI)	%	-0.3	12.2	48.7	<b>13.9</b>
Unemployment	%	7.2	9.3	9.1	<b>8.9</b>
Foreign direct investment	% of GDP	2.5	0.6	3.4	<b>3.7</b>
Export growth	%	-8.1	-14.2	-13.2	<b>-1.6</b>
Import growth	%	-3.5	-22.1	-17.9	<b>8.4</b>
Current account balance	\$ M	-16518.0	-4596.0	-189.0	-
Public debt	% of GDP	40.5	70.3	79.3	<b>81.2</b>
External debt	\$ M	149104.0	129020.9	121332.1	<b>117983.2</b>
Total debt service	\$ M	37848.4	20862.7	28587.5	<b>14773.6</b>
Net lending/borrowing	% of GDP	-4.3	-4.8	-1.5	-
Tax revenue	% of GDP	17.6	17.3	20.5	-
Government consumption	% of GDP	19.3	19.5	18.9	<b>19.4</b>
Public education spending	% of GDP	6.6	5.9	-	-
Public health spending	% of GDP	4.2	3.6	-	-
R&D expenditure	% of GDP	0.8	0.6	0.6	-
Military expenditure	% of GDP	2.4	3.0	4.0	<b>3.7</b>

Sources (as of October 2017): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

## 7 | Organization of the Market and Competition

Essential elements of a market economy are in place in Ukraine, although abuse of market power has been rather common.

Most prices are formally liberalized. According to the European Bank of Reconstruction and Development (EBRD), Ukraine's price liberalization enjoys a score of 4 (scale: 1 to 4+) since 1997. In September 2016, the government temporarily abolished remaining administrative price regulations on food products to test the

Market-based  
competition

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market response. It is expected that regulations will be permanently canceled in early 2017.

Utility, energy and telecommunication tariffs are regulated by designated regulatory bodies. The independence of the energy market regulator was strengthened in 2016. In 2015 to 2016, energy prices were increased to cost-covering levels in order to abolish cross-subsidization and stimulate energy saving.

Market entry has become easier. According to Doing Business (DB) 2017, Ukraine is ranked 20th in the category of “starting business,” a tremendous increase compared to the 76th position it held two years earlier. However, bankruptcy procedures remain tough. Ukraine is ranked 150th out of 190 economies in this category, moving down two spots compared to the previous report. The cost of bankruptcy is still much higher than the regional average, while the recovery rate is low.

Ukraine’s national currency – the hryvnia – is not fully convertible. Ukraine adopted the current account convertibility under the IMF’s articles in 1997, but foreign investors still face currency control difficulties.

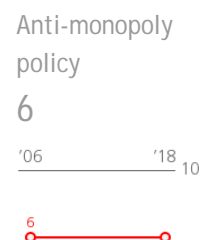
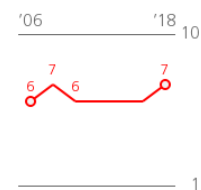
Foreign companies registered with local authorities receive important guarantees: (a) foreign investment cannot be nationalized or subject to requisition, except for force majeure, and in this case investors have the right to restitution of losses; and (b) investors have the right to unimpeded repatriation of profits, dividends and investments themselves after all taxes due are paid. In 2014 to 2015, the NBU applied a temporary restriction on purchases of foreign currency for the repatriation of dividends to control the currency crisis. These limitations were partly abolished in 2016 against the stabilization of the balance of payments.

The size of the shadow economy started to decrease in 2015 to 2016, compared to its peak in 2014. According to estimates by the Ministry of Economic Development and Trade, the shadow economy was at 38% of GDP in the first half of 2016.

Formally, competition rules are the same for all market participants, although enforcement can vary as the economy promotes the dominance of financial and industrial groups. A comprehensive judiciary reform launched in mid-2016 is expected to improve this situation.

Key competition laws are in place in Ukraine. There are also several public bodies responsible for the prevention of unfair competition and for the facilitation of competitive practices. The key authority is the Anti-Monopoly Committee of Ukraine (AMCU), established in 1994. Price setting in energy, utilities and telecommunications is regulated by respective national commissions and special regulatory bodies.

The responsibilities of the AMCU include the prevention of unfair competition and abuse of market power, control over concentration and collusion, control over price



setting in natural monopolies, and the protection of competition in public procurement.

The AMCU is controlled by the president of Ukraine, and reports to the Verkhovna Rada. As for other public institutions, since 2005 a public (advisory) council has exercised public control over the AMCU's activities. The council is comprised of 38 members representing Ukraine's major industry associations and NGOs.

In 2015 to 2016, in line with Ukraine's commitments under the Association Agreement with the EU, some important shortcomings on the part of the AMCU, such as lack of transparency and accountability, were addressed as follows:

- the AMCU started publishing its decisions online;
- an official clarification of the methods for setting penalties for anti-competitive practices aligned with the respective guidelines of the European Commission was passed by the AMCU;
- Parliament adopted a law simplifying concentration practices that harmonized with EU norms.

Also, the Law on State Aid was passed in 2014, aligning the system with the EU norms. The law makes the AMCU the responsible authority for monitoring and authorizing state aid, assessing its impact on competition and recovering unlawfully granted aid. Most of the norms will be enacted in mid-2017.

However, despite legal changes, enforcement remains very weak. According to the Global Competitiveness Report 2016-2017, Ukraine is ranked 136 out of 138 countries by "effectiveness of anti-monopoly policy."

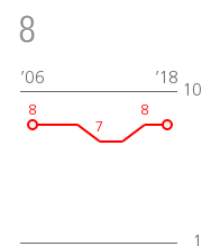
Ukraine's foreign trade is sufficiently liberal, although some exceptions exist.

The country has been a WTO member since 2008. Also, it signed free trade agreements (FTAs), including multilateral CIS FTAs and bilateral FTAs with all CIS members, an FTA with EFTA, a Deep and Comprehensive Free Trade Area (DCFTA) agreement with the EU and an FTA with Canada. Negotiations are also ongoing with Turkey and Israel.

The DCFTA agreement with the EU, Ukraine's largest trade partner, was provisionally enacted in 2016 (the full ratification depends upon a decision by the Netherlands).

For imports of agricultural products, the average most-favored-nations applied tariff rate is 9.2%, while for non-agricultural goods it is 3.7%. The majority of import tariffs are ad valorem. Ukraine uses only one global tariff quota, for raw cane sugar. The

Liberalization of foreign trade



DCFTA with the EU includes plans for tariff-rate quotas (TRQs) with duty-free in-quota imports for selected agricultural products.

Export duties are applied to only a few products, including some oil seeds, live animals, raw hides, natural gas and metal scrap. The rates have been significantly reduced as part of the framework of implementation of the WTO commitments.

Import and export licenses are required for a limited number of goods, and their number is declining. Currently, the licensing is applied predominantly for trade in ozone-depleting substances. The list of goods requiring licenses for foreign economic transactions is adopted annually by the cabinet of ministers.

The number of quantitative export restrictions was reduced in 2015 to 2016. In particular, there are no more restrictions on exports of slag, ash and residues containing mainly copper or zinc, and natural gas.

At the same time, in 2015, Ukraine introduced a ten-year ban on exports of unprocessed timber. The decision raised EU concerns since this ban is discriminatory and in violation with the DCFTA provisions.

Ukraine progressed in reforming trade-related measures that could constitute non-tariff barriers to trade. Aiming to use opportunities provided by autonomous trade preferences and the DCFTA with the EU, Ukraine significantly facilitated harmonization of its technical barriers to trade and sanitary and phytosanitary-related regulations.

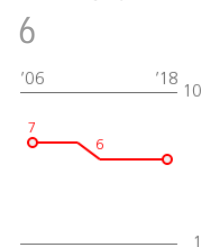
Ukraine has a two-tier banking system with the National Bank of Ukraine (NBU) as a supervisory and regulating body and commercial banks that serve economic actors and private households. The independence of the NBU was reinforced in 2015 in line with IMF requirements.

As of January 1, 2017, there were 96 licensed banks; over 80 banks left the market or were withdrawn by the NBU for violations of banking supervision requirements. In December 2016, “Privatbank,” the largest private bank in Ukraine, was nationalized after its owners refused to meet recapitalization requirements.

Foreign participation in Ukraine’s banking system was down to 38 banks compared to 51 in early 2015. At the same time, the share of foreign statutory capital was about 50% compared to 32% two years ago.

The main indicators of the banking system remained quite low, although there were signs of improvement. According to the NBU, the capital to assets ratio (the adequacy of regulatory capital) reached its minimum, at 7.09% in October 2015 (the WB reported 8.0% in 2015), after which it started to improve. As of January 2017, the ratio was 12.7%.

Banking system



According to the NBU, the share of non-performing loans is very high and reached 30.5% in December 2016 as more and more banks were forced to reveal the actual quality of assets and form adequate reserves. That is comparable to the WB assessment of non-performing loans at 28% in 2015.

In 2014 to 2016, international banking standards were gradually introduced in Ukraine. The changes include new requirements regarding internal audits (2014), more demanding capital requirements (2015), increased transparency of bank ownership structure (2015), increased responsibility of bank owners (2015) and new regulations on consumer lending (2016). Further changes are foreseen by 2020 in accordance with the Comprehensive Program of Financial Sector Development passed in 2015.

After almost two years of decline, the banking system started to attract deposits. Both demand deposits and deposits with up to two years till maturity increased in 2016, while longer-term deposits continued to decline.

The amount of outstanding loans declined in 2016 by 3.6% for the corporate sector and 11.9% for households, against a background of slow economic recovery and more stringent bank supervision requirements.

The stock market remained stagnant.

## 8 | Currency and Price Stability

The introduction of inflation targeting signified a very important shift in the country's policy paradigm. After years of debates, the decision was officially announced in early 2016. For 2016, the CPI target was set at 12% +/-3%. The aim is to achieve an inflation rate of 5% +/-2% from 2019 onwards.

According to the Ukrstat, in December 2016, CPI was 12.4% year-on-year, thus significantly decelerating in comparison with 43.3% a year before. The announced inflation anchor is among the factors that contributed to inflation deceleration, although likely it was not the most significant one.

Over the course of 2015 to 2016, the national currency lost about one third of its value despite rigorous temporary control measures imposed by the NBU. The devaluation was faster in 2015, while in 2016 the situation stabilized, which allowed the NBU to gradually liberalize the market, although many restrictions are still not abolished (e.g., mandatory sales of a fraction of foreign currency receipts).

Ukraine continued its cooperation with the IMF. The five-year Extended Fund Facility Program was signed in March 2015, replacing the stand-by arrangements settled a year earlier. By the end of 2016, Ukraine received three tranches amounting to SDRs 5.4 billion out of programmed SDRs 12.3 billion. The schedule of disbursements was uneven due to ups and downs in the structural reform process in the country.

Anti-inflation /  
forex policy

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In 2015 to 2016, the government aimed at ensuring macroeconomic stability by fiscal consolidation and a debt burden reduction. These reforms were in line with recommendations by the IMF, cooperation with which was renewed in 2014 and extended in 2015 through the extended fund facility.

The consolidated fiscal balance (without bank recapitalization and transfers to Naftogaz) diminished from 4.5% of GDP to 1.6% in 2015 and 2.1% in 2016.

On the revenue side, tax reform was introduced in 2016. Key changes include unifying personal income tax at 18%, reducing and unifying social security contributions (SSCs) to 22%, expanding the corporate income tax base due to the reduction in SSCs, and introducing a general VAT regime to agriculture.

On the expenditure side, important changes include a reduction in subsidies to state-owned enterprises, fiscal decentralization and public procurement reform. An introduction of compulsory online, above-threshold purchases for all state institutions allowed for more efficient and transparent usage of public funds.

Energy-sector reforms, including changing energy prices to cost-recovery level, facilitation of energy efficiency measures and a shift in gas purchases from Russia to the EU market, removed the need for fiscal transfers to Naftogaz. In 2014, Naftogaz ran a deficit at 5.5% of GDP, while in 2016, it is estimated to have had profit of about 1% of GDP.

To relieve debt pressure, external debt payments were restructured in 2015. The deal envisaged a 20% haircut, a prolongation of debt maturity and a grace period until 2019. As a result, at the end of 2015, public and publicly guaranteed debts stabilized at 79% of GDP. As of November 2016, total debt amounted to 77% of GDP, but the nationalization of Privatbank increased the debt obligations of the state to almost 84% in December 2016.

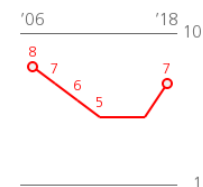
## 9 | Private Property

The constitution of Ukraine and the Civil and Commercial Codes guarantee the right to private property. However, property has been weakly protected due to deficiencies in the judicial system and pervasive corruption.

According to the Global Competitiveness Report 2016-2017, Ukraine did not improve the protection of property rights: the country is ranked 131st out of 138 countries for property rights and 125th out of 138 for intellectual rights protection. At the same time, according to Doing Business 2017, Ukraine moved 39 positions up to 70th place in the category “protecting minority investors.”

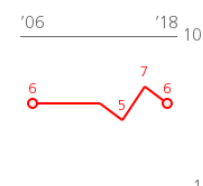
### Macrostability

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### Property rights

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In 2015 to 2016, important efforts were taken to strengthen the rule of law and the protection of property rights, although the impact is still to be seen.

Key anti-corruption institutions became operational, including the National Anti-Corruption Bureau (NABU), the Special Anti-Corruption Prosecutor's Office and the National Agency for Prevention of Corruption.

In mid-2016, a comprehensive reform of the judicial system was launched, featuring greater independence of and higher accountability for judges. The changes are to be implemented within three years.

Also in 2016, a law strengthening protections for investors came into force. The new law includes the introduction of a derivative suit as a new mechanism for protecting investors' rights and the establishment of an "independent directors" institute.

Also, legislation was amended to fight corporate raiding at the end of 2016. Key changes include:

- Mandatory notarization of signatures on statutory documents and the decisions made at general meetings of stakeholders;
- Increased liability for state registrars;
- Registration of property rights only in the region where the property is situated;
- Notification of owners regarding any actions to be taken with regards to their property.

Also, a reform of the system for the protection of intellectual property rights was launched.

Private enterprises accounted for about 63% of Ukraine's economy in 2012, according to the Ministry of Economic Development and Trade of Ukraine.

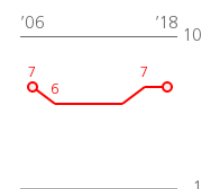
The role of the state is still important in several spheres like energy (Naftogaz) and transport (railways). The state has made changes to the governance structure of state-owned companies (SOEs). Corporate management of SOEs became more powerful, as did their accountability and efficiency.

In 2016, a law simplifying the privatization process and increasing its transparency was passed. An online platform – privatization.gov.ua – was introduced for efficient and transparent privatization of smaller entities.

However, large-scale privatization remained stalled. The state focused too much on the sale of the Odessa Portside Plant that failed because of lack of investor interest, largely due to a high indebtedness and litigations associated with the enterprise. Consequently, other sales were postponed.

Private enterprise

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The SME sector is large and expected to become one of Ukraine's economic growth drivers. According to Ukrstat, SMEs and entrepreneurs accounted for over 99% of Ukraine's private sector enterprises in 2015, for 79% of jobs, as well as for 63% of total sales. These figures have been gradually growing.

## 10 | Welfare Regime

The social safety net is well developed and consists of two main components: services and money transfers.

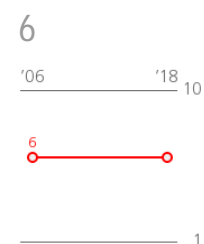
The key element of the social safety net is a pension system. The pension system should consist of three pillars, but in actual fact only two are functioning: the solidarity system (first pillar) and a non-state pension provision system based on voluntary participation (third pillar), although the development of the latter is limited by a weak stock market, low incomes and mistrust in financial institutions. Pension reform launched in 2003 was not completed, as the second pillar – compulsory individually funded pension insurance – was not introduced.

According to Ukrstat, in 2016, there were 12.3 million pensioners in Ukraine, 29% of the total population. The ratio of employed working-age people to pensioners was about 1:3. The pension fund's expenditures in 2016 were UAH 254 billion, or about 11% of GDP. The fund's own revenues constituted only 43% of its needs, while the rest was covered by a transfer from the central budget (in 2015, the fund's revenues covered 73% of its needs). The higher transfer compensated for the twofold reduction in the social contribution rate to 22%, aimed at stimulating business activity and de-shadowing of the economy.

Despite the large size of the pension fund, actual pensions remain very low. In 2016, the average pension was UAH 1,700 or about \$64 per month, while the minimum wage was UAH 1,247 or \$47 per month. Therefore, pensioners have remained among the most vulnerable groups of population.

Subsidies are another important component of the social safety net in Ukraine. In 2015-2016, social protection expenditures continued to grow and reached 31% of total consolidated fiscal expenditures in 2016 (about 10% of GDP). The increase is largely explained by the energy-sector reform, namely the introduction of market-level energy prices for households, which resulted in the elimination of cross-subsidization, but led to a surge in the cost of utility bills to consumers. To mitigate negative social consequences, the procedure for acquiring the housing and utility subsidies was simplified. As a result, by the end of 2016, the number of households that received these subsidies reached 6.1 million or 40.5% of the total number of households, while the average subsidy was UAH 1,104 (the average wage in 2016 was UAH 5,070).

Social safety nets



Public expenditure on health was about 3% of GDP in 2015-2016. According to the constitution, health care is to be provided universally, efficiently and free of charge. However, de facto Ukraine's health care system does not provide universal access to quality health care: spending patterns are inefficient and informal payments are common.

Ongoing Russian aggression in Donbas significantly worsened social protections in the territories not controlled by the Ukrainian government. People living in occupied territories do not have proper access to social welfare payments, and provisions of other social services are at least partly disrupted.

Ukraine has established the legal framework for protection against discrimination, both in the constitution and in specific laws. The Law on Principles of Prevention and Countering Discrimination in Ukraine was passed in September 2012. The country has also joined international anti-discrimination conventions. However, implementation of legal provisions against discrimination remains insufficient, resulting in inequality and social exclusion faced by some social groups.

Gender inequality is moderate. According to the Human Development Report 2015, Ukraine is in group one, comprising countries with high equality in HDI achievements between women and men.

According to WB Development Indicators, the adult literacy rate of females is higher in Ukraine than of males (95.1 vs. 92.4). All children are involved in primary and secondary education (gross enrollment at 103.9% and 99.2% respectively). The enrollment in tertiary education is lower at 82.3%, but still comparatively high. There is no gender discrimination in access to education. The ratio of female to male enrollment is 1.0 for primary and secondary education, and 1.2 for tertiary education.

In the Gender Inequality Index 2014, Ukraine is ranked 57th out of 154 countries. Females have equal access to education, the social protection system and labor force participation, but tend to receive lower wages and be severely underrepresented political life. Female participation in the labor force has remained stable at 49% of the total labor force.

According to the Global Gender Gap Report 2016, produced by the World Economic Forum, Ukraine is ranked 69th out of 144 countries with a 0.700 score, which is worse than two years ago (56th out of 142 states with score 0.706, but still within the margin of error). Ukraine continues to have a very low rating in the political empowerment of women.

Social exclusion exists for some ethnic minorities, like Roma, which involves exclusion from education, the labor market and social services.

Disabled people and people with HIV/AIDS have unequal access to participation in society, including access to education and employment. People with disabilities

Equal opportunity

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frequently remain excluded due to deficiencies in both urban and rural infrastructure, namely a lack of adaptation of buildings, roads, transport, et cetera. The exclusion of people with HIV/AIDS is largely due to the stigma associated with HIV status and prejudices among the population.

The annexation of Crimea by the Russian Federation in March 2014 significantly worsened the protection of rights of Tatars in the region and forced many to resettle in mainland Ukraine.

## 11 | Economic Performance

In 2016, Ukraine achieved macroeconomic stabilization after several years of decline. Real GDP returned to a growth trajectory, inflation was curbed and current accounts and the budget balance became manageable.

Real GDP is estimated to have increased by around 2% in 2016 compared to a 9.9% decline the year before. The recovery was investment-driven: gross capital accumulation is estimated to have grown by 20% compared to a much more moderate expansion in household consumption (+4.4%).

Inflation considerably decelerated. The CPI growth was 12.4% year-on-year in December 2016 compared to +43.3% a year ago.

The current account deficit remained manageable at 3.7% of GDP in 2016, although it expanded compared to 2015 due to a launch of the DCFTA with the EU, the cancellation of a temporary import surcharge and a revived internal demand, which together stimulated imports.

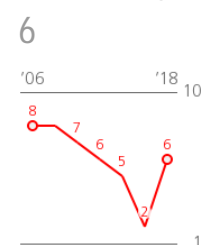
The fiscal consolidation policy allowed for a reduction in the consolidated fiscal deficit from 4.5% of GDP in 2014 to 1.6% in 2015 and 2.4% in 2016. The introduction of mandatory online public procurement significantly contributed to transparency and efficiency in public expenditures.

In 2015, the government successfully restructured its foreign debt obligations to remove immediate financial pressures and gain time for structural reforms. The deal includes a 20% haircut on the principal (about \$3.6 billion), an extension of maturity and a change in the payments schedule from 2015-2023 to 2019-2027. These arrangements allowed the country to improve its short- to medium-term financial sustainability.

As of November 2016, the state debt amounted to \$57 billion or about 66% of GDP. The nationalization of Privatbank pushed the debt up to about 72%.

Unemployment remained at the 2014 level, accounting for around 9% of the economically active population aged 15-70 (ILO methodology).

Output strength



## 12 | Sustainability

In 2016, Ukraine was ranked 44th out of 180 countries in the Environmental Performance Index (EPI). Its score was 79.69. This is a considerable improvement over the previous ranking.

The Association Agreement with the EU has brought a new impetus to environmental policy. The commitments of Ukraine are quite extensive, although long-term.

In 2015, the country ratified two important international environmental protocols, namely the Protocol on Strategic Environmental Assessment to the Convention on Environmental Impact Assessment in a transboundary context and the Kyiv Protocol to the Aarhus Convention (regarding the European Union's monitoring system of environmental pollution).

In 2016, several draft laws related to environmental commitments were developed. Two – on environmental impact assessment and on access to ecological information – were adopted by parliament but vetoed by the president at the end of 2016, who requested that the parliament create laws that are more functional and without loopholes. The revised draft laws are expected to be passed in 2017.

The National Strategy on Waste Management and the National Plan for Reduction of Emissions have been drafted.

In 2015, Ukraine significantly reduced the level of pollution (e.g., the amount of produced waste dropped by 12% and CO2 emissions by 15%). But the reduction is likely explained by lower economic activity rather than more stringent implementation of environmental norms.

The system of incentives for environmentally friendly behavior is imperfect. The increase in energy tariffs in 2015 to 2016 became a positive stimulus for energy saving and switching to alternative sources of energy. At the same time, penalties for violation of environmental legislation are tiny, creating no incentives to follow the rules.

There is an established system of state and private education and training in Ukraine. Primary and secondary education is provided for everybody including citizens, foreigners and stateless persons. Public expenditures on education declined to 5.6% of GDP in 2016 as compared to 6.4% in 2014.

According to the HDI for 2014, the gross enrollment rate for primary education was 105.5%, for secondary education 98.9%, and for tertiary education 79%. The adult literacy rate remains well above 90%. Expected years of schooling stabilized at 15.1 years.

Environmental policy

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Education policy / R&D

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According to the Global Competitiveness Report 2016-2017, Ukraine improved its ranking in several education-related indicators. The country is ranked 56th out of 138 countries in the quality of its educational system and 27th in the quality of math and science education. However, the ranking for primary education declined from 40th to 51st within two years indicating a need to reform this sector. Also, on-the-job training remains quite weak. The country is ranked 94th for the extent of staff training.

Recently, Ukraine slightly improved its rating related to technological readiness. The Global Competitiveness Report 2016-2017 places Ukraine at 93rd out 138 countries for availability of latest technologies, and 74th out of 138 for firm-level technological absorption. Insufficient protection of property rights and low expenditures on R&D hamper innovations in Ukraine. Financing of R&D measured as a share of GDP has been less than 1% of GDP.

## Governance

### I. Level of Difficulty

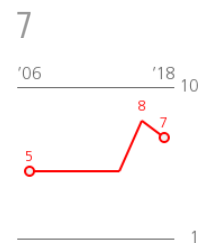
Ukraine faces several long-term structural constraints. It is undergoing a severe demographic crisis, characterized by an aging and shrinking population. According to the Ukrainian Statistical Service, the average life expectancy in 2015 was 66.4 years for men and 71.4 years for women. At 1.5 children born on average to each woman (2015), the country's fertility rate is insufficient to ensure the natural recovery of the population. This creates future economic and social problems. At the same time, Ukraine is a country of labor emigration. Several million Ukrainians work (temporarily) abroad, mainly in the European Union and Russia.

So far, policies and institutions have been ill-equipped to deal with the consequences of these developments, which include higher expenditures for health care, care for the elderly, pensions and a shrinking labor force.

The country's energy-dependent and energy-inefficient economy poses an additional structural constraint. Although, on a positive note, since 2014 Ukraine reduced its gas consumption and diversified its energy supply, so that in 2016 for the first time the entire gas supply came from the territory of the EU (and not from Russia, which previously held a monopoly).

A new structural constraint that arose in 2014 has remained acute. The annexation of Crimea and the armed insurgency, coupled with military intervention in Donbas, resulted in a number of important problems for Ukraine: loss of control of about 12% of its territory (excluding Crimea), losing access to mineral resources and mines (the latter responsible for electricity shortages); 9,758 people killed and 22,779 injured in the conflict between April 2014 and December 2016, according to the U.N. Human Rights Monitoring Mission in Ukraine; over 1.7 million internally displaced persons (according to official statistics). All this puts additional pressure on social safety nets; and has broken production links. Moreover, Ukraine does not control part of its border with Russia, through which support to pro-Russian fighters is supplied regularly. This means that military operations in Donbas will continue, creating an unprecedented level of expenses for the army, which in turn places constraints on a budget already exhausted by economic crisis.

Structural  
constraints



Civil society traditions date back to pre-Soviet times. During the Soviet era, civil society was suppressed and controlled by the party state. Some major human rights organizations, such as the Ukrainian Helsinki Human Rights Union or the Kharkiv Human Rights Protection Group, have their roots in the Soviet human rights movement. The same applies to some charitable foundations.

In recent years, popular acceptance of and involvement in civil society has improved and since 2014 the level of trust in civil society has exceeded the level of mistrust, unlike all the years since independence. Due to Euromaidan and its aftermath, more people have shown a willingness to protest and to become volunteers. Although only about 10% of officially registered Ukrainian NGOs work on a steady basis and they mostly depend on support from outside agencies, their societal and policy influence has increased. Civil society has become aware of its role in the reform process and has improved its advocacy activities through joining forces in networks and NGO coalitions, working closely with international institutions that foster reforms in Ukraine and exercising increased pressure on public authorities.

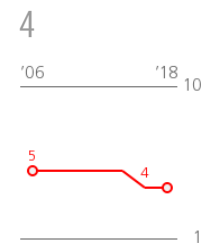
Even though Ukraine is an ethnically, linguistically and religiously diverse country, conflicts of ethnic, linguistic or religious origin remain insignificant. None of Ukraine's five major churches constitutes a state church. Ukraine has liberal laws regarding religion, which also guarantee freedom of religious practice. Ukrainian, Russian and other languages are freely spoken in Ukraine and there are many examples of people from different ethnic backgrounds taking governmental posts or become members of the parliament and local councils.

The conflict in Donbas might appear to contradict this statement at first glance. However, it was only to a very limited degree provoked by social, ethnic or religious cleavages. Rather it was initiated by (irregular) Russian insurgents and has been sustained to the present day by Russian military involvement with support from local fringe politicians and criminal elements, often closely associated with former President Yanukovich and his Party of Regions.

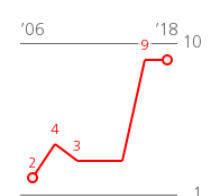
The nature of politics in Ukraine is only partially confrontational. Only two parties – the Opposition Block and that Yulia Tymoshenko Block, which are in opposition and enjoy more support than other parties due to their populist agenda – are interested in early elections. However, the majority of parliament is not interested in losing seats and President Poroshenko is not interested either, so the scenario is improbable. The ruling coalition often needs additional votes to pass laws, so a lot of bargaining with members of parliament from outside the coalition and the business interests behind them takes place. The opposition parties have so far failed to mobilize the sections of society affected by social difficulties for any meaningful protests.

In principle, there is no potential for a serious conflict beyond the one in Donbas. Risks emanate from the fact that, since the war in Donbas illegal, circulation of weapons has increased in Ukraine. Experts talk about up to five million pieces of

#### Civil society traditions



#### Conflict intensity



weaponry (among a population of 42 million). Moreover, the Minister of the Interior, Arsen Avakov, officially granted so-called reward weapons to 4,708 persons and in January 2016 there was an incident with a member of parliament who injured a person with one of these weapons. Another potential source of societal tension could be the large number of internally displaced people in different regions of Ukraine, although they are welcome all over Ukraine and numerous volunteer initiatives help them to survive and adapt.

## II. Governance Performance

### 14 | Steering Capability

There is a discrepancy between formal arrangements and practice. Formally, as of the beginning of 2015, reforms in Ukraine have been guided by five different documents:

First, Strategy 2020, a document developed by the administration of the president and adopted in January 2015, includes 60 priorities, covering a broad spectrum of reform areas.

Second, following the early parliamentary elections in October 2014, the Coalition Agreement, adopted by the parties forming the parliamentary majority, includes 17 reform areas, which are supposed to overhaul the entire system of governance in Ukraine.

Third, the Action Plan of the Government, adopted in December 2014 and updated when the change of the cabinet took place in April 2016, claims to take into consideration Ukraine's international obligations and refers to the Coalition Agreement as an integral part of its plan.

Fourth, Ukraine's Memorandum with the IMF, is considered another document guiding domestic reforms along with, fifth, the EU-Ukraine Association Agreement.

The National Reform Council (NRC), established in 2014 with the help of international actors, attempted to bridge the gaps among the documents and become a platform for coordination among different actors. It defined 18 reform areas and developed priority objectives based on all five documents and reports about their implementation on a regular basis. However, the council does not have decision-making powers and has failed to become a platform for mediating among the interests of different stakeholders and setting strategic priorities.

In reality, decision-making is often guided by short-term political considerations. The president had to devote a great deal of attention to preserving power because of

Question  
Score

Prioritization

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partners defecting from the government coalition, resignations by ministers and an enduring conflict with the oligarch and former governor of Dnipropetrovsk, Ihor Kolomoisky. Many observers are of the opinion that longer-term strategies and goals are forced upon the government by external actors like the IMF and the EU, as well as by Ukrainian civil society.

The administrative and civil service reform, launched in May to June 2016, lays down foundations for important changes. In late 2016 to early 2017 the position of state secretaries was introduced in all ministries and respective professionals were selected through competition. These positions are supposed to be responsible for institutional memory of the ministries irrespective of political changes. Moreover, there is a plan to introduce reform divisions in each and every ministry that will be responsible for long-term strategic planning. It will take time before the relevant provisions are in place and become operational, but the first steps have been taken.

The results of the reform process implemented in 2015 to 2016 are rather mixed. The NRC, in its report covering nine months of 2016, identified a number of objectives that were implemented and several that were not. Positively, the NRC provides comprehensive factual information on the implementation of various reforms, making the process more transparent.

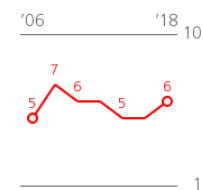
Civil society assessments are often more critical. The regular independent expert reform assessment initiative – Index for Monitoring Reforms (iMoRe) – states that the pace of reforms implemented in the course of 2015 to 2016 was mostly below an acceptable level. During this period of time, the assessment noted the greatest progress in the sphere of fighting corruption, and somewhat less in reforms of the banking and energy sectors. Other reforms, notably the reform of the judiciary and of the civil service, decentralization and reforms to state enterprises have been lagging.

The civil society platform, Reanimation Package of Reforms, has also been critical, although it identified 17 real reform successes by November 2016 in fighting corruption, increasing transparency (including in public finance), health care, education, decentralization, and reforming the energy and security sectors. The latter assessment also recognized legislative achievements related to civil service reform and that of judiciary, although implementation is yet to occur.

Since the Revolution of Dignity in 2014, policy learning processes and practices have improved significantly. This has to do with the influx of people from the private sector, academia and civil society to top positions in some ministries and other state institutions. Many ministers and specialists in the post-Revolution governments speak fluent English, which was never the case previously. This gives hope that the expertise from outside the old system will have a lasting impact on the work of the government.

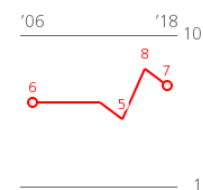
#### Implementation

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#### Policy learning

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Moreover, Western donors in many ways guide and support the reform process with expertise, personnel and funding. This has partially helped to solve the problem of low salaries in state institutions, since donors fund some expert positions in ministries. The donors also invest a lot of resources in capacity building and the development of procedures (such as internal electronic systems for the circulation of documents) that ensure more efficient exchanges of information and decision-making.

One of successful example is the state company Naftogaz, which before 2014 accounted for 25% of state budget expenditures, but by 2016 already accounted for 10% of budget revenues. This has been attributed to, among other things such as lower energy prices, the replacement of management and profound gas sector reform. However, a more critical view holds that subsidies to private households have not really changed as they have been moved from Naftogaz to the state budget. Moreover, the company's profit came exclusively from transit fees paid by Russia.

The launch of administrative civil service reform in May to June 2016 lays the foundation for improving policy learning at different levels of bureaucracy, which will however take years to show results. At the same time, it has to be noted that some of the more experienced and prominent pro-reform actors have resigned in frustration.

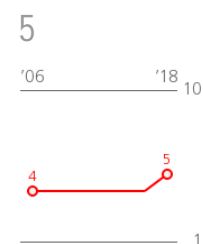
## 15 | Resource Efficiency

In 2015 to 2016, the efficiency of the use of the government resources in Ukraine increased. Special efforts were made to improve the use of financial resources of the state. The government undertook a fiscal consolidation that allowed reducing the consolidated fiscal deficit (without bank recapitalization and transfers to Naftogaz) from 4.5% of GDP in 2014 to 1.6% in 2015 and 2.1% in 2016, outperforming IMF program targets. Moreover, the energy sector reform and improved corporate governance of SOEs, in particular in Naftogaz, allowed for closing one of the most serious fiscal gaps.

Successful public procurement reform was implemented, in particular by making online procurement mandatory for all above-threshold public purchases. It allowed not only for saving public funds, but also for stimulating competition and fighting corruption through higher transparency and accountability of operations. Also, public procurement of medicines and medical instruments was delegated to international organizations to end corruption and increase efficiency in spending.

Fiscal decentralization allowed local communities to target their needs better, also contributing to efficiency in public expenditures.

Efficient use of assets



Public service reform, envisaging open and competitive selection of public servants, was launched in 2016, but it will take time to complete it. Meanwhile, many public institutions (ministries, public services, the central bank, et cetera) were reorganized to optimize their functions and staff needs.

The system of policy coordination improved in the course 2014 and 2015 and remained improved in 2016. Due to a return to the parliament-president form of governance, the coalition government has better opportunities to coordinate its policy objectives with interests represented in parliament. Yet this cooperation has not been completely successful, with many government initiatives having been rejected by parliament.

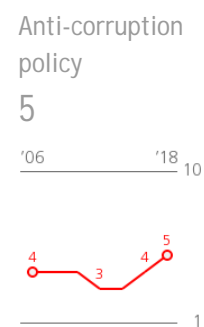
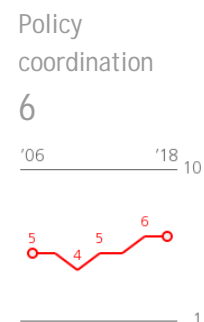
The biggest innovation was the creation of the NRC under the leadership of the Office of the President. It brings together key decision-makers, including the president, the prime minister, the chairman of the parliament, ministers and chairs of parliamentary committees, as well as representatives from civil society. In 2015, the NRC held 17 meetings. However, in 2016, the number of meetings declined: only five meetings took place. This may reflect that the NRC's capacity to advance reforms is limited, since it has no decision-making powers. Moreover, it has limited capacity for achieving cross-party agreements. However, at the very least it provides a platform for discussion and its website contains comprehensive information about the reform agenda as provided in various documents, the progress made and public perception.

Another positive step was the introduction of the position of deputy prime minister for European and Euro-Atlantic Integration in April 2016, which potentially might help to improve intra-governmental integration.

In actual fact, however, the bulk of policy coordination is provided for by informal arrangements and personal connections among representatives of different institutions.

Fighting corruption is perceived as a priority reform objective by experts, the international community and society at large (according to public opinion surveys). Therefore, there has been a lot of pressure on politicians to implement reforms in this area.

Although with a lot of resistance and slowly, important reforms in this area have been initiated. For instance, three anti-corruption institutions were set up, all of them independent, with employees hired by an impartial and professional selection committee with the participation of civil society. The National Anti-Corruption Bureau (NABU) as a major body to combat high-level corruption was set up and started operations in December 2015. Between December 2015 and September 2016, the Bureau launched 245 investigations and passed 31 cases on to the courts (due to the unreformed judiciary the cases were not pursued). Introducing a special Anti-Corruption Court that would eliminate this problem is still envisaged. The other two



institutions are the Special Anti-Corruption Prosecution Office, which works closely with NABU, and the National Agency on Preventing Corruption, which is in charge of the state's anti-corruption policy and declaration of assets by officials. By August 2016, 45 million UAH were confiscated and returned to the state budget in the course of investigations.

Another important step was the introduction of the online public procurement system ProZorro in February 2015. As of September 2016, all public procurements are conducted within the system. Due to the functioning of the system, experts estimate that potentially over 6 billion UAH have been saved for the state budget since the system was launched. ProZorro was awarded the prestigious international Procurement Leader Award.

Not least, in September 2016, an electronic system for declaring assets was launched, whereby all civil servants and politicians have to declare their assets. The real implications of the system will be felt in autumn 2017 when it will be possible to detect inconsistencies between official incomes and declared assets.

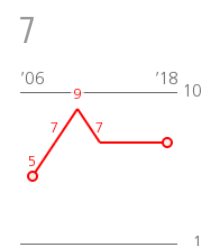
These initiatives lay down the basis for a comprehensive anti-corruption policy, although at the moment it is too early to say that the level of corruption in Ukraine has significantly diminished.

## 16 | Consensus-Building

Rhetorically, all actors are committed to the principles of democracy and a market economy. Moreover, the president, the parliamentary coalition and both governments formed by it supposedly represent Euromaidan and its values; that is the reason for overhauling the old system of governance and development to replace it by a more democratic and transparent system based on the rule of law. However, in reality, what can be called the “democratic camp” is rather diverse, with many members representing the old system and its values and engaged in various networks with vested interests.

In addition, there are other groups of actors who resist the reform process. First, oligarchs who prefer the old rules of the game, including a poor business climate aimed at preventing competition from smaller domestic businesses and foreign investors, poor rule of law, and a politically controlled judiciary. Second, political parties with a populist agenda that are interested in early elections, such as the Opposition Block (mostly composed of members of the former Party of Regions) and the Yulia Tymoshenko Block, who currently enjoy relatively high support. Third, resistance comes from many potential losers in the reform process, such as civil servants or judges from the old system who will leave once reform is underway. Yet,

Consensus on goals



strong pressure for reforms from new actors among public authorities, civil society and international donor community also play an important role in pushing for reform.

Formally, there is a consensus among the key political actors that Ukraine should have a market-based economy as strategic long-term goal for the country. However, there are acute debates about the ways to achieve that goal. It is expected that the Association Agreement with the EU, signed and ratified in 2014, will provide an important anchor for market-based reforms in the country and limit the space for maneuver for the actors who veto reforms.

One can best describe the situation in Ukraine as a struggle between actors who push for and pursue reforms and those who are interested in preserving the status quo and continuing to benefit from the old system. The line dividing both camps is not clear cut and authorities and actors who claim to be democratic often play the role of veto players for various reasons: preservation of power or privileged access to resources, links to particularistic informal interests and fear of transparency and competition. Therefore, the result of reform efforts since Euromaidan has been patchy and too slow, according to expert opinions.

But still Ukraine has never seen so many reforms as during the past three years, since independence. Democratic actors among public authorities are in a minority; but due to combined pressure from these actors, civil society and international actors, reforms succeeded in some areas. Particularly reforms succeeded where new institutions were created, as opposed to old institutions being reformed. Some examples include the new patrol police force free of corruption and staffed with new professionals, anti-corruption institutions, the electronic public procurement system ProZorro and the electronic declaration of assets, among other reforms. Many succeeded not least because they were a part of conditions set forth by international institutions.

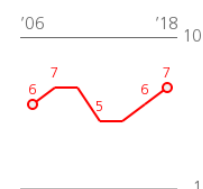
In a separate development, the Russian-backed fighting in Eastern Ukraine has enhanced the political significance of near-criminal local elites and marginalized groups with clearly an anti-democratic agenda.

Two large cleavages can be observed in Ukraine today. One of them has to do with the military conflict with Russia, which is perceived somewhat differently by different segments of society. Another has to do with the implications of the reform process and the economic crisis (for instance, since 2014 the tariffs for household gas increased by 700% and the Ukrainian national currency is worth three times less than it was previously), the latter situation having been exploited by populist political parties and politicians.

Concerning the first cleavage, while in Western and Central Ukraine the majority of population consider the conflict in Donbas a Russian plot, in South and Eastern Ukraine and in Donbas itself, most people think that both countries share responsibility. In the south, 18% even think that the conflict is primarily Ukraine's

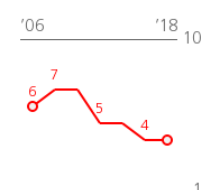
Anti-democratic actors

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Cleavage / conflict management

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fault (opinion poll conducted by the Democratic Initiatives Foundation and Razumkov Center, May 2016). Public opinion is also divided as to the compromises Ukraine should make to achieve peace, as to Ukraine's policy toward the occupied territories and the conditions under which elections there could take place. Some parties like the Opposition Block regularly claim that Ukraine's policy toward Donbas was too aggressive.

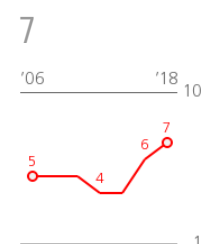
In January 2017, Viktor Pinchuk, oligarch, philanthropist and fourth richest man in Ukraine, published an article in the Wall Street Journal in which he argued that Ukraine should drop the goal of NATO accession and make additional compromises so as to attain peace in Donbas. This opinion provoked a lot of indignation in Ukrainian social networks, showing how emotionally charged this issue is. It is for this reason (the sensitivity of the issue) that the political leadership has avoided taking any steps that would give special status to the temporarily occupied territories and pave the way for elections there, as envisaged in the Minsk Agreement, and despite strong international pressure to do so.

As to the second cleavage, in 2016, there were protests by people who allegedly lost money when some banks were closed and by those protesting against rising tariffs. In December 2016, 46% of population supported the idea of early parliamentary elections and 37% did not support it; the first group was stirred up by political parties that became popular by criticizing government policies – the Opposition Block and the Yulia Tymoshenko Block. By contrast, government policy regarding these issues seeks to soften these dividing lines, by avoiding radical steps, relying on mediation from international partners and communicating the ongoing achievements of the reform process (as well as by providing subsidies to vulnerable groups).

In the years following Euromaidan, civil society has become an increasingly important force for driving the reform process. Although the authorities do not always take civil society opinions into consideration, international actors and donors cooperate closely with civil society and this joint pressure from outside and from below, known as “sandwich effect,” makes it almost impossible for the authorities to eschew change. Important reforms introduced since Euromaidan became possible due to such pressure.

Additional factors have to do with civil society's increased expert and advocacy capacity and the presence of reformist actors in government positions who themselves come from civil society. Thus, civil society representatives are involved in various consultation groups and advisory bodies with the authorities and even the human resources departments for some reformed public authorities. Increased transparency in decision-making, public finance, the life styles of politicians and the ownership of media create a better environment for civil society to have an impact.

Civil society participation



One of the most recent conflicts took place during Euromaidan, and resulted in the deaths of over 100 people – mostly protesters, but also several in the police force. Society demands that these incidents be investigated and those who gave the orders to kill and those who followed these orders be brought to justice. However, until the present the investigation and attempts to bring those under suspicion (by July 2016, 187 law enforcement representatives were declared under suspicion) to justice have proceeded slowly. The prosecution has failed to work in a coherent manner, while in the courts many judges represent the old system.

Ongoing conflicts concern the situation in Crimea and Donbas. While Crimea is now de facto under the control of the Russian authorities, the fighting in Eastern Ukraine has produced human rights violations and war crimes perpetrated by both sides, according to OSCE reports. Not least due to exposure to Russian media, people in the territories that were freed from the insurgency still have mixed loyalty toward the Ukrainian state. These fresh wounds have to be better understood and dealt with.

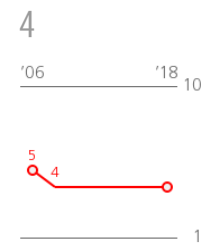
The Ukrainian government filed declarations with the International Criminal Court, which gave the latter limited jurisdiction to open a preliminary examination into alleged crimes both related to Maidan and to Crimea/Donbas.

With respect to historical injustices in Ukraine – mostly related to Stalinist or Nazi crimes – most of these have not yet been discussed comprehensively or systematically. In April 2015, a formal “decommunization” process started after laws were approved which, among other acts, outlawed communist symbols. In January 2017, the Institute of National Remembrance of Ukraine announced that in the course of 2016, 51,493 streets and 987 cities and villages were renamed, 25 administrative regions were renamed and 1,320 Lenin monuments and 1,069 monuments to other communist figures were removed as a part of decommunization. Moreover, since December 2015 three Communist parties were banned. This was inevitably met by disagreement among political actors and segments of the population in Eastern Ukraine, where Soviet nostalgia is still present. Other historical events that are not perceived equally across Ukrainian territory are those of Holodomor and the status of World War II veterans who did not fight on the side of the Soviet army, but rather with the Ukrainian Insurgent Army (Ukrayins’ka Povstans’ka Armiya, UPA).

## 17 | International Cooperation

Since the end of Euromaidan, the authorities of Ukraine have been very sensitive to support from outside. Economic crises and Russian aggression, against the background of a weak state, put Ukrainian authorities in a situation in which international assistance was needed to survive and stay afloat. Given this and the lack of a tradition or institutions for long-term strategic planning, as well as the system of

Reconciliation



Effective use of support

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coordination of international assistance, international actors have played the driving role in defining reform objectives.

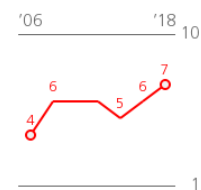
In 2015 to 2016, the government made significant efforts to streamline international assistance, as well as to increase its transparency and efficiency. An important achievement was that the Ministry of Economic Development and Trade (MEDT), which is responsible for coordination of international assistance, in December 2016 launched the pilot version of the online system - <http://openaid.gov.ua/> - which facilitates coordination.

According to MEDT, as of 2016, the EU was the largest donor to Ukraine, with the highest contributions done by the EIB (\$5.9 billion), the EU Delegation (\$0.6 billion) and the European Atomic Energy Community (\$0.6 billion). The EBRD contributed \$5 billion, and the U.S. government about \$1 billion. Efforts to institute better governance, civil society and social infrastructure development and education attract most of the donor support. Apart from that, the IMF plays a crucial role in setting the reform agenda.

The use of technical assistance remains in line with general policy objectives, but the absorption capacity of the state remains quite low. Intra-government coordination has not been smooth and subsequent efficiency in using international aid will depend on implementation of civil service reform and decentralization, among others.

Ukraine's credibility with international actors has increased since the transition of power after Euromaidan, yet with certain reservations. On the one hand, Western partners are aware of the fact that, after the Revolution of Dignity, Ukraine received a unique chance to make a reform breakthrough and provided sizable financial (grants and loans) and technical assistance to support Ukraine on this path. Ukraine, for its part, demonstrated readiness to pursue required reforms. The country managed to quickly organize free and fair elections to elect a new president, a new parliament and local authorities in 2014 to 2015. It swiftly signed and ratified the Association Agreement with the EU and developed structures to ensure its implementation. To some extent, reform-minded leaders were elected into parliament and assumed high-level positions in the government. Finally, the president and prime ministers managed to avoid political infighting, which was one of the mistakes made by the Orange Revolution authorities. The leadership also managed the coalition and government crisis in February to March 2016, with the appointment of the new government in April 2016 that has built on the work of the previous two post-Maidan governments. Ukrainian authorities have also increased the transparency of their work and their openness toward cooperation with civil society.

On the other hand, Western partners are well aware of the constraints and resistance to reform that stem from the old, deeply rooted "captured state" system. They are also aware of the fact that the current Ukrainian authorities are mostly old elites linked to informal, self-serving networks. These factors account for the slow pace of reforms





and, knowing this, Ukraine's international partners have strengthened their conditionality and targeted criticism of the authorities, thus having increased their pressure.

To sum up, the credibility of the Ukrainian government has been mixed, having to do with the fact that different actors and forces, which either promote or block reforms, drive its work. Given this, international partners have reacted with policies that have a good mixture of support and pressure.

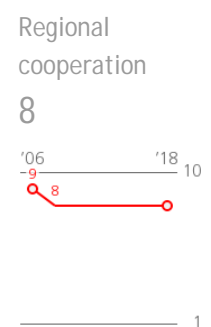
Ukraine aims at having good relations with all neighboring countries. Ukraine is a founding member of the Commonwealth of Independent States (CIS) and a member of GUAM (Georgia, Ukraine, Azerbaijan and Moldova), the Organization of the Black Sea Economic Cooperation (BSEC) and of the Central European Initiative (CEI). While GUAM was founded primarily to balance Russian influence in the region, with not much of an impact, other organizations mostly serve as platforms for political elites to meet and exchange opinions.

On a pan-European scale, Ukraine is a member of the Council of Europe and the OSCE. Ukraine also expressed interest in cooperation with and even membership in the Visegrad Group (the Czech Republic, the Slovak Republic, Poland and Hungary) and the Weimar Triangle (Germany, France and Poland), but this so far has been limited to a few negotiations.

Ukraine's relations with Russia have undergone a dramatic transformation since March 2014, when Crimea was annexed and the conflict in Donbas started. Russia failed to drag Ukraine into the Eurasian Economic Union (EEU – Russia, Belarus, Kazakhstan, Armenia and Kyrgyzstan) and to prevent signature of the Association Agreement with the European Union. The aggression forced Ukraine to fortify its border with Russia and boost its military power.

Public opinion with respect to EEU versus European Union integration has seen a constant increase of support of the latter. In December 2013, 47% of citizens favored access to the EU and 36% preferred the EEU, in December 2016 only 11% favored the EEU, while support for the EU increased to 58%. Ukraine has been cooperating with many Western neighbors, particularly Poland and the Baltic states, whose support of Ukraine's European Union integration and firm stance on sanctions against Russia has played an important role. There are cross-border cooperation projects with Poland, Hungary, Slovakia and Romania, mainly within the framework of the European Neighborhood Policy and the Eastern Partnership.

Ukraine's cooperation with countries of the Eastern Partnership (in addition to Ukraine, the initiative includes Moldova, Belarus, Georgia, Armenia and Azerbaijan) remains intensive. Although this cooperation was and is still driven by the European Union with little initiative from the ground, it serves as a forum for socialization among officials, civil society and other actors from the six countries.



## Strategic Outlook

Since the end of the Revolution of Dignity in early 2014, Ukraine has experienced a reform impetus previously unseen, although resistance from the old system and structures has also been high. Thus, in 2015 to 2016, the struggle between “the old” and “the new” was unfolding very actively, and this situation will persist. Hardly any of the post-Maidan reform achievements can be seen as sustainable in the sense that they have surpassed the point of no return. Many of them are in the form of legislation or new institutions, while full-fledged implementation still has to follow. Some crucial reforms, such as that of the civil service or the judiciary, are at an initial stage and will require years to succeed. The share of reformers among the authorities is still rather limited. But these reformers inside the state structures serve as key partners of the civil society and international actors who push for reforms from outside.

Given the fragile situation with reforms and constant attempts by populist and anti-democratic actors to destabilize the situation, using the disillusionment within society, it is important for all reform-minded actors to better consolidate their efforts and to better communicate their achievements to society. This means that the ruling elites need to lead by the example of following democratic rules, including the separation of business and politics and strict implementation of transparency rules to fight corruption. Further change in the composition of the political elites should be promoted to engage more new professionals.

Implementation of the civil service, administrative and judiciary reforms should be a priority, since those are responsible for implementation of decisions and their enforcement, which eventually will provide sustainability to reform achievements. Civil society representatives, young professionals and external experts should play a greater role not just in specific reform projects, but also in policy-making and political debates in general. The consolidation of the political party system should be enhanced to promote sustainable program-oriented parties, instead of the political projects of prominent individuals.

International actors should continue using conditionality as leverage to push for reforms and further enhance the capacity of civil society, young political parties, alternative trade unions, media and other social actors, especially at the local level, who challenge the old system and offer a way forward. In the longer term, a new generation of politicians, civil society activists, experts and journalists need to be trained, supported and promoted to decision-making positions. The EU in particular should understand that the success or failure of Ukraine will serve as a strong indicator of the feasibility of democratic reforms in the whole region of the Eastern Neighborhood, and also in Russia.

It is unlikely that the situation in Donbas will become calm in the near future, and it is even more unlikely that Russia will return Crimea to Ukrainian jurisdiction. There is a deeply held conviction in Ukraine that the key to the solution is mostly in Russia's hands and that, for this reason, international actors should not entertain the idea of lifting sanctions on Russia, but rather come up

with a strategy for dealing with the long-term security threat that Russia presents to the entire European continent. Whether the Minsk II Agreement provides a feasible roadmap for conflict resolution has become ever more questionable. The original timetable is already null and void. It is clear from the Ukrainian perspective that any measures that infringe on the country's sovereignty and territorial integrity will hardly be acceptable by the public and therefore will not receive official consent, be it in the form of special status for the territories in question or local elections under the current circumstances.

At the same time, the international context will require more self-awareness and self-confidence on the part of Ukrainian citizens. The growth of populism and anti-democratic trends all over the world, the possible concentration of the U.S. and Europe primarily on domestic issues requires that Ukraine rely more on itself and its efforts to secure the democratic achievements attained by the Revolution of Dignity so as to ensure the irreversibility of reforms.