A dangerous pause. Why Ukraine’s cooperation with the IMF has stalled – interview with IMF Resident Representative Gösta Ljungman

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Gösta Ljungman, IMF Resident Representative in Ukraine, told NV about how actions of Volodymyr Zelenskyi and of justices of the Constitutional Court impact on the cooperation program with the IMF.

In 2020, Ukraine was confronted not only by the COVID crisis of external origin but also an internal crisis the official Kyiv is responsible for. This is cooperation with the IMF: in June, after the adoption of laws on the banking and land markets, the country signed a new USD 5 billion stand-by cooperation program with the Fund and even managed to obtain USD 2.1 billion. However, the matter went no further.

Volodymyr Zelenskyi’s criticism of supervisory boards in state-owned companies, his staff decisions, and lack of progress in anti-corruption efforts provoked this “pause”. As a result, in the difficult COVID year, Ukraine is again unable to obtain the full financing from the IMF.

And with this, the Constitutional Court (CCU) has decriminalized false e-declaration by MPs and public officials, thus calling into question the possibility of further cooperation with the Fund.

What should the country now expect from the IMF, and what does the Fund expect from the official Kyiv? NV talked about this to Gösta Ljungman, IMF Resident Representative in Ukraine.

Q: The Ukrainian government regularly emphasizes that Ukraine is on the right track in fulfilling the IMF requirements in order to get the next loan tranche. What are the prospects of positive developments in the Ukraine-IMF relations?

A: To answer this question, it is worthwhile to pause for a moment and consider what the purpose of the Fund-supported program is. A key objective of Fund-supported programs in Ukraine is to move ahead with structural reforms to resolve problems that hold back investment and therefore prevent sustained and inclusive economic growth.

This agenda includes reforms aimed at eliminating corruption, restoring confidence in the judiciary, reforming tax and customs, and improving the efficiency of state-owned enterprises. A second objective is to maintain macroeconomic stability. Ukraine did a lot to restore financial, fiscal and external stability in the years after 2014. But it paid off.

Strong fundamentals have supported growth and put Ukraine in a good position to deal with the current Covid-related global crisis. The Fund-supported program is therefore aimed at preserving responsible fiscal, monetary, exchange rate and financial sector policies. But there is no denying that the Covid pandemic requires a strong response to protect lives and livelihoods. So a third objective of the program is to ensure that sufficient resources are available for health care and
temporary support for individuals and business, and also that these resources are used effectively.

To achieve all of these objectives, Ukraine has made a number of commitments—described in detail in the Memorandum of Economic and Financial Policies—that it will honor during the course of the program. Unfortunately, since the approval of the program, there have been several developments that run counter to those commitments. But, we see a strong interest from the Ukrainian authorities to continue with the Stand-By Arrangement, and we are in close discussions on how to ensure that key institutions are preserved, fiscal policy is sustainable, reforms move forward, and macroeconomic and financial policies are prudent. Once there are clear assurances on all these fronts, it will be possible to proceed with reviews of the program.

Q: The Constitutional Court passed a massively criticized ruling on e-declarations. Besides, legal status of the National Anti-Corruption Bureau as well as the National Corruption Prevention Agency is under question now, given all the latest court rulings. How critical is it for the Ukrainian leadership to address those issues in order to secure positive cooperation with the IMF?

A: Successfully fighting widespread corruption is arguably the most important issue in Ukraine. Not only is this something that the Ukrainian people demand and deserve, but it is also necessary to attract investment, both domestic and foreign. Corruption is holding back growth in Ukraine. It is for this reason that the creation of the anti-corruption infrastructure—NABU, High Anti-Corruption Court, asset declarations, criminal liability for illicit enrichment, SAPO—has been at the core of Fund-supported programs since 2014. Preserving and strengthening the anti-corruption framework is a key element of the current Stand-By Arrangement and is a necessary condition to proceed with the program. A weakened anti-corruption framework is not consistent with the objectives of the Fund-supported program.

Q: What do you expect next from the NBU? What are the IMF recommendations on NBU’s regulatory and monetary policies, staff decisions, preserving its independence at the current moment, given that deputy governors Kateryna Rozhkova and Dmytro Solohub are de facto stripped of their powers?

A: Let me again take a step back and try to explain how central bank issues have been reflected in the current and previous Fund-supported programs. The independence and institutional capacity of the National Bank have been at the core of Fund-supported programs and technical assistance. This has covered the separation of the National Bank from political decision making, which is a key dimension of independence, the reorientation of monetary and exchange rate policies to inflation targeting and a floating exchange rate, the clean-up of a banking system ravaged by fraud and excessive risk-taking, the development of staff competence, and the restructuring of the organization and decision-making to ensure checks and balances and well informed policies.

The transformation of the National Bank since 2014, which put in place a functions-based organization, and committee-based decision-making, has been nothing short of impressive. The preservation of the central bank model put in place during 2014-19—including governance arrangements—and central bank policies has been a key contributor toward maintaining macroeconomic stability and is a key commitment under the Fund-supported program.

Q: How realistic is it for Ukraine’s Finance Ministry to successfully conduct a necessary volume of borrowing this year in order to avoid cutting the budget-2020, in your view?
What do you think about Ukraine’s budget for the next year with projected fiscal deficit of 6% of GDP?

As I mentioned before, Ukraine—as all other countries—has to find a balance between the need to support its population and economy during the COVID-crisis and maintain long-term macroeconomic stability. The Fund-supported program set out a path for this, which involved a large increase of spending on necessary health care, and income support to individuals and business to bridge the loss caused by quarantine restrictions.

Once the pandemic ends, the program aims at bringing back expenditure to a level that can be sustained over the longer term. This program—which assumes that the fiscal deficit will be firmly put on a downward path starting in 2021—was and continues to be realistic and includes total financial support of around US$5 billion from the IMF, of which $2.1 billion was already disbursed in June. Unlocking the rest of that financing will depend on implementing the program and ensuring that commitments are honored.

Q: President Volodymyr Zelenskyi has a list of serious foreign policy accomplishments – it includes military cooperation with the UK, Turkey, successful EU-Ukraine summit. But he's criticized for his domestic policies. Do you see that his policies bring risk to Ukrainian macroeconomic stability?

A: I will not comment on politics outside the Fund-supported program.