At a Glance

- The economy grew modestly by 2.4% in the first half of 2017, and poverty remains higher than pre-crisis levels. Boosting economic growth to 4% or more in the next two years is critical to reducing poverty and improving living standards, which will also require progress on ambitious reforms in land markets, the financial sector, anti-corruption, and privatization, to stimulate investment and productivity.

- Despite higher revenues, the fiscal deficit may exceed the target of 3% of GDP in 2017 due to higher public sector wages and spending on social programs. Reducing the fiscal deficit in 2018 and beyond will require adopting responsible pension reform and implementing education and health reform that improves the quality of services while optimizing the school and hospital network.

- Moderate poverty in 2016 is estimated at 26.5%, down slightly from 27.5% in 2015, but up sharply from 14.1% in 2013. The poverty rate in 2016 is estimated at 7%, up sharply from 3.3% in 2013.

Country Context

Ukraine has experienced acute political, security, and economic challenges during the past three years. Since the “Maidan” uprising in February 2014 that led to the ousting of the previous president, the country has witnessed several momentous events, including the outbreak of conflict in eastern Ukraine and presidential, parliamentary, and local elections.

The Government, which took office in April 2016, has committed to continuing previous reform efforts, and a government program and action plan covering a wide-ranging reform agenda were issued in May.

Key reforms undertaken since 2014 include: carrying out significant fiscal consolidation, moving to a flexible exchange rate, reforming energy tariffs and social assistance, making public procurement more transparent, simplifying business regulations, stabilizing and restructuring the banking sector, adopting a health reform package, and establishing anti-corruption agencies and asset disclosures for public officials, all the while contending with powerful vested interests that continue to oppose reforms.

Although all of these are important steps, more needs to be done, including in other areas. Going forward, Ukraine will need to advance reforms on multiple fronts to achieve sustainable recovery and shared prosperity.
The World Bank and Ukraine

Ukraine joined the World Bank in 1992. Over the 25 years of cooperation, the Bank's commitments to the country have totaled close to US$12 billion in about 70 projects and programs.

In March 2014, after receiving a request from the Ukrainian Government, the World Bank Group immediately announced its support for a reform agenda aiming to put the Ukrainian economy on a path to sustainability. The current International Bank for Reconstruction and Development (IBRD) portfolio consists of eight investment operations of roughly US$2.5 billion and one guarantee of US$500 million.

The World Bank recently endorsed a 2017–21 Country Partnership Framework (CPF) for Ukraine that supports the country’s efforts to achieve a lasting economic recovery to benefits all the entire population. The new CPF focuses on ensuring that markets work more effectively, establishing the necessary conditions for fiscal and financial stability, and improving service delivery for all Ukrainians.

Key Engagement

Responding to the crisis in Ukraine, in March 2014 the World Bank Group announced that it would provide additional financial and technical support to the country. Since 2014, the World Bank Group has supported the people of Ukraine through two series of development policy loans (DPLs), seven new investment operations, and a guarantee amounting to approximately US$5.5 billion aimed at improving critical public services, supporting reforms, and bolstering the private sector.

The World Bank has supported high-priority reform measures to address the key structural roots of the current economic crisis in Ukraine and to lay the foundation for inclusive and sustainable growth through two series of budget support operations: the multi-sector DPL series

WORLD BANK PORTFOLIO

No. of Projects: 8 IBRD investment operations, plus one guarantee
Total Lending: $2.5 billion, including $148 million from the Clean Technology Fund (CTF)


Reform measures supported by these four budget support operations promote good governance, transparency, and accountability in the public sector, as well as stability in the banking sector; a reduction in the cost of doing business; and the effective use of scarce public resources to provide quality public services at a crucial time. These operations also support the authorities in continuing to reform an inefficient and inequitable housing subsidy system while protecting the poor from tariff increases by strengthening social assistance.

World Bank investment projects have focused and will continue to focus on improving basic public services, such as district heating, water and sanitation, health, and social protection, as well as public infrastructure, such as the power transmission networks and roads. The Bank is also supporting Ukraine through policy advice and technical assistance in formulating and implementing comprehensive structural reforms.

In addition to financing several ongoing private sector projects, the International Finance Corporation (IFC) is implementing a large advisory program in the country, working to simplify regulations, improve the investment climate and energy efficiency, boost the completeness of local food producers, help open new markets, and increase access to finance.
Recent Economic Developments

Economic growth remains modest due to the unfinished structural reform agenda and headwinds from the conflict in eastern Ukraine. Real GDP grew by 2.4% year-on-year (y-o-y) in the first half of 2017, following growth of 2.3% in 2016. Although the resumption of growth is a positive development, it represents a weak recovery since it follows a cumulative 16% contraction in 2014 and 2015. Even key sectors exhibiting relative strength, such as manufacturing, trade services, and transport, continued to grow at a modest pace—3.7, 3.5, and 4.4%, respectively—in the first half of 2017, which is insufficient to drive stronger growth in the overall economy.

The mining and utility sectors contracted by 6.6 and 5.5%, respectively, due to the trade blockade against uncontrolled areas of the Donbas region, which affected coal, steel, and electricity production. On the other hand, construction and fixed investment continued to exhibit strong growth in the first half of 2017—at 26 and 22%, respectively—pointing to strengthening investor confidence in some areas, although both remain down sharply from pre-crisis levels. Merchandise exports grew by 23% in the first half of 2017.

Fiscal expenditures and revenues grew strongly in the first half of 2017, with the supplementary budget adding to expenditure pressures for the rest of the year. In the first half of 2017, both expenditures and revenues exhibited strong growth. Expenditures were up by 13.5% in real terms due to the increase in the minimum wage (and resulting higher wages for teachers, doctors, and civil servants), as well as higher spending on social programs. Revenues also grew strongly by 22.8% in real terms in the first half of 2017, driven by higher revenues across the board, including personal, corporate, and value added tax, as well as social security contributions and non-tax revenues. As a result, the fiscal balance in the first half of 2017 amounted to a surplus of 0.9% of full-year GDP. However, the supplementary budget adopted in July 2017 adds to expenditure pressures for the rest of the year, including higher spending on the military, social programs, and capital investment, leading to a fiscal deficit in 2017 that may exceed the target of 3% of GDP. At the same time, the public debt level continued to grow, reaching 85% of GDP as of July 2017 due to the high cost of bank recapitalization.

Economic Outlook

The growth projection for 2017 remains modest at 2%, but progress on the ambitious package of reforms under consideration could accelerate growth to 4% or more going forward. The growth outlook is affected by two key factors. First, Ukraine faces continued headwinds from the conflict in the Donbas region as evidenced by the coal and trade blockade with the uncontrolled areas. Second, the authorities have been working on an ambitious package of reforms to address structural bottlenecks and advance growth prospects. The next few months are a critical window of opportunity within which to lock in these important reforms.

Establishing a transparent market for land transactions would enable Ukraine to tap its vast potential for agricultural exports. Strengthening the governance of state-owned banks and introducing measures to streamline the resolution of nonperforming loans (NPLs) would enable a gradual resumption of lending to the private sector.

Deeper anti-corruption reforms, further improvements to the business environment, and progress on privatization would strengthen investor confidence and attract foreign investment. Locking in these reforms in the next few months could raise growth to 4% or more in the next two years, an outlook subject to serious risks, however, related to progress on reforms in a complex political environment and a possible escalation of the conflict or deterioration in the external environment.
Project Spotlight

Anti-Corruption Reform

Anti-corruption reform in Ukraine, supported by the DPL, means that officials must now declare their wealth online. During the first wave of e-declarations, over 100,000 officials revealed their wealth, and overall, around US$1 billion in the form of cash and bank accounts was declared—the equivalent of nearly one IMF tranche to Ukraine. If this money were declared in 100 hryvnia bills, the cash would cover 684 square acres, reach 16 miles in height, and weigh 259 tons.

E-declarations have exposed a vast difference between the fortunes of politicians and those of the citizens they represent. Some officials have declared millions of dollars in cash, while others have declared ownership of fleets of luxury cars, expensive Swiss watches, diamond jewelry, and large plots of land, despite the fact that the average salary in Ukraine is just over US$200 per month. Declarations have been made not only by senior authorities in Ukraine but also by regular officials across the country.

Over 70 criminal proceedings are currently ongoing, related to the illicit enrichment of the declarants or the lies in their e-declarations. E-declarations are the first step on the road to the full transparency of the political elite. The next step is accountability. E-declarations were established with World Bank support and became a key instrument in helping create a comprehensive system of corruption prevention in Ukraine.

Corruption in Ukraine is a threat to national security and undermines the well-being of citizens. Although public access can raise valid concerns, the benefits outweigh the costs and any interference with privacy rights in the declaration is proportionate to the public interest. Online disclosure of public declarations has been introduced in many countries and is essential if public servants are to be held accountable.