

DAVID LIPTON: “UKRAINE CAN’T PAUSE OR GO BACKWARDS”

Interview of David Lipton, IMF First Deputy Managing Director, to Ukrainsky Tyzhden Weekly

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Ukraine completed 3 out of 11 structural benchmarks from the previous memorandum with the IMF, and still received the last tranche of the loan. Why did the IMF grant it?

We always try to see the big picture. Ukraine is making important strides in stabilizing and building foundation for growth in the country. It was time to go ahead. But we still want all of the other benchmarks to be implemented. We continue our work with the government on some high-priority reforms necessary for the next review. If we move forward together, Ukraine can overcome the legacy of the last 25 years and really make life better for a lot of people in the country.

The upcoming benchmarks include some politically sensitive ones, such as pension and land reform. How would the IMF put pressure on the Ukrainian Government to go through these reforms taking into consideration the fact that Ukraine is looking at double elections in 2019?

We don't force anyone to do anything. The history of the past 25 years in Ukraine shows that the country moves forward when it wants to do so, and it doesn't when it can't find agreement.

The next three important steps are pension reform, land reform and privatization of state enterprises. These reforms are all long overdue. Not doing them has imposed costs on Ukraine year in and year out. You have some of the most fertile land in Europe. But it has never been possible to reap full benefit from it given the land use and ownership. I remember discussing it with then-President Kuchma! It's time that this reform is done, because Ukraine can no longer afford to be giving up what it is giving up now. Ukraine will have to decide. The Prime Minister has declared that he aims to try to do it.

When you talk about privatization, I also remember meeting with top officials, including the Privatization Minister, already in 1995 to discuss their plans. Again, the cost of poor management, poor financial outcomes in state enterprises over the many years since then is substantial. Ukraine can improve its economy if it begins and carries out the process of privatization. If you look around Eastern Europe, many countries that have successfully privatized have found benefits in doing so. It is up to Ukraine, and if Ukraine wants to do it, we will support it.

Pension reform is always a sensitive issue, affecting many people. But no one in Ukraine can possibly like the fact that the average pension now is so small. And Ukraine cannot afford higher ones, because there are too many pensioners. There has to be some rationalization. The Prime Minister has assured us that he intends to try to craft a pension reform that would get the backing of the people.

The people of Ukraine – and the Parliament on their behalf – have to ask themselves whether they want to move on those three reforms and what is the cost of not doing so. If nothing changes, we will have more and more years of difficulties and waste that have characterized the past.

Pension reform has been mentioned in many memoranda of Ukraine's cooperation with the IMF since 2015. Yet, virtually no progress has been achieved. We have some discussions or concepts, but not a complete reform ready to be implemented. Can Ukraine suggest anything as an alternative in case it does not carry out this reform?

We have discussed pension reform with the President and Prime Minister since the beginning of this program. We never contemplated that it would happen at the beginning of it. The first part of the program focused on stabilizing the financial situation and bring finances under control. That has been done.

Ukraine is now in phase two, where it needs to solidify stability and prepare base for growth and more efficient operation of the economy. Therefore, it is now time for pension and land reforms, and privatization. This kind of reforms will create the basis for development and growth in the country, and make the future different from the past.

The Prime Minister has explained his aims and intentions and expressed his commitment. We hope that the Ukrainian people and Parliament can come together with the Prime Minister behind the very meaningful pension reform – It is very important for the country's finances, budget, people and the economy. It is a necessary next step.

Head of the IMF's mission to Ukraine Ron van Rooden published an article on pension reform. It was heavily criticized by Deputy Prime Minister Pavlo Rozenko. This hints at some interests at the highest level which are unlikely to back the reform.

All big complicated reforms are controversial; they don't just happen; they require a lot of planning, discussion, dialogue, even argument. The aim is to get a sensible pension reform that makes the system financially sound but also provides meaningful pensions to people who receive them, rather than pensions that are a pittance and not fair to the people who worked their whole lives.

The Government is expected to submit a draft law on land reform to Parliament by the end of May. However, we have yet to see any discussions on that whatsoever. Would the IMF be flexible about this deadline?

The IMF team has been visiting Ukraine, and we will have conversations with the authorities in the coming days and weeks to develop a strategy. We want to see the pension reform, land reform and privatization.

When it comes to privatization, we have seen two years without any success. What should be done to go through that dead point?

There needs to be a decision to go ahead. Ukraine clearly has state enterprises that would be valuable private companies. There have been some companies prepared for privatization that for various reasons have not been privatized. And while I understand some of those reasons, these are certainly valuable companies. In private hands, these companies would be more productive and profitable, and hence serve the Ukrainian people better.

It takes a combination of political decision and careful preparedness. There are examples of successful privatization efforts in the region. IMF has the expertise and some of your neighbors have the expertise. There are plenty of ways to figure out how to do this well, if there is a decision to go forward.

With the resignation of Valeria Gontareva as NBU Governor, the number of bright reformers continues to shrink in Ukraine. This being said, does the IMF expect obstacles in cooperation with Ukraine?

Governor Gontareva has done a fantastic job in an incredibly difficult situation, despite huge resistance from some people and political factions. When she came in, the country was on the edge of instability: It had an exchange rate system that had contributed to paralyzing exports and growth. Moreover, Ukraine had many banks that were either or both mismanaged and failing. She has dealt with those problems and deserves a medal for it, as far as I am concerned.

After all of the hard work she has done, one can understand her moving on. Running the National Bank of Ukraine has never been and is not an easy job. But there is no doubt that Ukraine can and will find someone to carry forward the good hard work that she has done.

Do you expect the restructuring and privatization of Ukrainian state-owned banks to be included in the Ukrainian program with the IMF at any point?

Already some of the state banks are being dealt with. It is certainly a subject of interest for us.

In two years, Ukraine is expected to start making large payments on foreign debt. That will coincide with the period of elections. Meanwhile, Ukraine does not have substantial economic growth to meet those financial needs. Do you expect any financial problems caused by that in two years?

We see growth returning to Ukraine after several years, reaching over 2 percent. If the program goes forward, that growth rate can rise. But much more importantly, if Ukraine continues to succeed, solidify stability and intensify growth, then capital markets will make funding available more amply and on better terms. In that circumstance, there would be no problem. But if Ukraine decides to pause or step back from reform, there will inevitably be a problem.

Two other important reforms are of the state fiscal service and customs. Virtually no progress has taken place there. And the ex-head of the State Fiscal Service was arrested. Do you expect that Ukraine can start moving in the right direction after that move?

I surely hope that Ukraine addresses the problems in those two areas. It would be a very important progress.

In the second half of 2016, Ukraine passed the e-declarations law. Lately, however, controversial amendments have been made in it. Fighting corruption is a major part of Ukraine's program with the IMF. How do you assess Ukraine's progress in that?

Ukraine is moving forward in fighting corruption, though not fast enough. There are many dimensions to fighting corruption. Part is about having institutions – part of that was the creation of NABU envisaged in the program. Part of that is transparency – the e-declarations address it. Part of it is enforcement – that is a domestic governance issue, and the President and the Government have to take it seriously. Part of it is cleaning up problems in banks – corruption in many countries comes from the ability of oligarchs to use banks to fund corrupt activities or for companies to make illicit payments through financial institutions. Wherever banks have been managed and governed well in Eastern Europe, corruption has lessened.

Finally, part of fighting corruption is about liberalization. One of the greatest epicenters of corruption in Ukraine was the gas system. Cleaning up Naftogaz and its system, adjusting the prices so that there are no opportunities to buy the imported gas low and sell high – these are the ways for cleaning up corruption.

In some of these areas, Ukraine has made quite important steps forward. In others, there is a lot more to do. Some of these areas we can try to foster and support. Some require political action by the leadership of the country.

If you were asked to assess the success of Ukraine's reforms in general, taking into account accomplishments in the banking and gas sector reforms on the one hand, but lack of any in privatization on the other, how would you assess what is needed and what has been done in percentage?

IMF doesn't do report cards... Ukraine has performed an important stabilization of the economy. It is something that the leadership should be proud of and that people should understand. Sometimes, the

stabilization phase doesn't feel very good – it takes getting to the growth phase for people to start appreciating the value of the work that has been done.

In Poland, for example, there were a number of changes in governments after stabilization, and a number of years had passed before the population started to feel the benefits of transition when growth had risen.

While stabilization was a major accomplishment, there is an so much left to do. Ukraine can't pause or go backwards, or else it will lose the work that has been done. It should go forward because there is huge potential – provided that the rest of the reforms are completed – to develop the economy, to have growth and rising income. Then people will feel better about it.

When does the IMF expect for the global financial markets to open to Ukraine?

Markets have two sides – supply and demand. Right now, the interest of the capital markets is in providing funding to emerging markets. We have seen a number of countries, also those that don't have highest ratings, financed. But the other side matters as well: that Ukraine prepares itself, makes itself a good, worthy customer. Having completed the review with the IMF was a useful step. Making progress towards the next review could be just the ticket to convincing the world and markets that Ukraine is heading in the right direction.

Interviewer Lyubomyr Shavalyuk