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Tymoshenko 1 & 2

Despite the tug of war occurring between the parliamentary majority coalition and the opposition, it seems likely that Yulia Tymoshenko will return as premier. If the Tymoshenko-2 government remembers the lessons learned from the mistakes under Tymoshenko-1, and receive support from the parliamentary majority coalition to pursue reforms, then the Orange coalition will have an opportunity to make up for lost opportunities by reinvigorating the economy

Despite the tug of war occurring between the parliamentary majority coalition and the opposition, it seems likely that Yulia Tymoshenko will return as premier. This has elicited both applause and groans from political analysts. Therefore, the (impending) confirmation of the Tymoshenko-2 government is a good opportunity for us to investigate the successes and failures during Tymoshenko-1: the eight months she served as premier in 2005.

The biggest complaint against Tymoshenko-1 was that growth plummeted from 12 percent in 2004. After dismissing Tymoshenko almost 10 months ago, President Viktor Yushchenko suggested that during her tenure, there were “serious problems” regarding management of the economy. “Economic stability,” he said, could be restored “in two to three months.”

While “stability” may have occurred, economic growth did not. It is clear now that Ukraine’s economic slowdown in 2004 cannot be blamed entirely on Tymoshenko’s mismanagement. This can be seen from the lack of any noticeable improvement in growth under her successor, Yuriy Yekhanurov, who generally is widely praised for his management skills, and has served two months longer than Tymoshenko did.

There were, indeed, some significant mistakes made by Tymoshenko’s government in 2005 that should be avoided when Tymoshenko-2 returns in 2006. In particular, Tymoshenko and her cabinet sometimes spoke rashly and without thought as to how they would be interpreted by foreign investors.

The most important case in point is Tymoshenko’s statement in mid-February 2005 on her government’s re-privatization policy.

“We have coordinated the work of the government and the prosecutor-general,” she said. “And for each enterprise in which the prosecutor has discovered violations, we will put a specific program in place to put an end to all illegal transactions surrounding state property.”

Further, she repeated an oft-stated Orange Revolution slogan, promising “that which was illegally put into private hands” would be “returned to the state.” Although

Tymoshenko herself declined to provide the number of enterprises involved, or explain specifically what the “program” for dealing with these enterprises entailed, a spokesman for the Prosecutor-General’s Office later said 3,000 enterprises were being evaluated (but interestingly, did not say the enterprises would be re-privatized).

Tymoshenko’s statement, combined with the number provided by the PGO, was interpreted by some as a government decision to re-privatize 3,000 companies. Tymoshenko never made a concrete move to do so, and in fact, stated that any questions would be solved “through the justice system,” giving current owners the right to pay a legally determined price differential and maintain their property. She also denied that 3,000 companies were involved, but again declined to name a number. Therefore, although Tymoshenko never specifically said 3,000 enterprises would be re-privatized, she left her comments widely open to interpretation.

The then-prime minister’s vague statements, occurring at the same time as similarly vague statements on the issue from the presidential administration, frightened investors and provided fodder to Tymoshenko’s enemies in big business. It was an inauspicious start to Tymoshenko-1.

Tymoshenko-1 also intervened in the gas, meat, and sugar sectors in an attempt to control spiraling prices. These decisions concerned investors and provoked severe international criticism. Tymoshenko-2 should avoid repeating these pitfalls.

However, it is important to note that, in the meat and sugar sectors, the Tymoshenko government first attempted to increase imports and decrease custom duties in order to increase supply and decrease price. The Kuchma-era holdover parliament blocked each such attempt. In fact, in the sugar industry, the parliament actually decreased the level of imports allowed into the country. Prices immediately skyrocketed, while several parliamentary deputies with sugar interests benefited.

Nevertheless, the Tymoshenko-1 decision to ultimately intervene in the above industries was a major error. Instead of solving the problem, it led to further increases in price and decreases in supply. In these cases, the Tymoshenko-1 government exhibited limited understanding of market forces. Since then, however, Tymoshenko has admitted her mistake in attempting to manually control prices, taking on more new liberal economic advisors, and vowing not to do so again.

Despite these issues, there were other important factors that led to lower GDP growth rates for both Tymoshenko-1 and the Yekhanurov governments. These include a downturn in demand for Ukraine’s most important export, steel, and a drop in world steel prices.

Metals, energy and chemicals account for two-thirds of Ukrainian exports. These industries are energy intensive and therefore sensitive to increases in energy and transportation costs.

In addition, it is still unclear to what degree the 12 percent growth in 2004 was real. It is noteworthy that reliable polls in 2004 did not show Ukrainian voters felt they were living in a country experiencing a massive economic growth boom. The Rand

Corporation's Keith Crane, an expert on Ukraine's economy, believes that if statistical discrepancies are taken into account, the real decline in growth in 2005 was closer to 5 percent.

Some analysts also note that the economy in 2005 was nothing like the economy in 2004, when important industrial sectors were "managed" and assisted by "insider" government favors.

Foreign investor and consumer confidence was seemingly not affected by Tymoshenko-1. Retail trade boomed by 23 percent in 2005. At \$7.5 billion, Foreign Direct Investment also was the highest in any year since Ukraine achieved independence. Only \$4.8 billion of this is accounted for by the sale of Kryvorizhstal, a successful re-privatization that was prepared by Tymoshenko-1.

Other advances made under Tymoshenko-1 include the removal of tax exemptions for Special Economic Zones and improvement of customs enforcement leading to improved revenue collection.

The year 2005 also saw the first attempts by Tymoshenko-1 to realistically aim for WTO membership. Both Tymoshenko-1 and the Yekhanurov government can take credit for Ukraine being granted market economy status by the EU and U.S. in December 2005 and February 2006, respectively.

Rand's Keith Crane is critical of the lack of progress under Tymoshenko-1 on an economic code, a joint stock company law and land reform. Others criticize a failure to truly decrease bureaucracy and improve the tax code. But, the Yekhanurov government has also made limited progress on these items.

Between Tymoshenko-1 and Tymoshenko-2, Tymoshenko has attempted to improve her image by portraying a business-friendly face and respect for property rights. Nevertheless, while investors have come to accept the idea of another Tymoshenko government in the hopes that her well-known, energetic, workaholic nature will jumpstart stalled reforms, they remain cautious.

The mistakes made by Tymoshenko-1 should be criticized with a view to avoiding them under Tymoshenko-2. Nevertheless, Tymoshenko-1 produced important positive results and its record was far more varied than is often suggested by analysts. The lack of any economic upturn, coupled with increasing citizen disillusionment under the Yekhanurov government demonstrates that certain factors in the past two years were beyond the control of the government.

However, Tymoshenko-2, unlike Tymoshenko-1, will operate with a parliamentary coalition and without hostility from a Kuchma-era parliament. This factor alone should improve the working of the government.

Should the Tymoshenko-2 government remember the lessons learned from the mistakes under Tymoshenko-1, and receive support from the parliamentary majority coalition to pursue reforms, this caution will disappear. The Orange coalition then will have an opportunity to make up for lost opportunities by reinvigorating the economy.

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