

The World Bank in Ukraine Country Snapshot



An overview of the World Bank's work in Ukraine

April 2017

UKRAINE	2016
Population, million	42.6
GDP, current US\$ billion	92.6
GDP per capita, current US\$	2,174
Life Expectancy at birth, years	71.2

At a Glance

- The economy grew modestly by 2.3% in 2016, with a bumper agriculture harvest leading to stronger growth of 4.8% in the fourth quarter. Poverty increased significantly in 2015 but moderated slightly in 2016, due to lower inflation and the resumption of economic growth.
- Economic growth is projected to remain modest at 2% in 2017 due to headwinds from the global economic environment and the coal and trade blockade on the Donbas region in eastern Ukraine. Reforms to bolster investor confidence and competitiveness are needed to help growth pick up to 4% in the medium term.
- The World Bank is working with the Government of Ukraine to support high-priority reform measures to address the structural roots of the current economic challenges and to improve the provision of basic services to the people.

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 was 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 over US\$10 billion in about 70 projects and programs.

In March 2014, after receiving a request from the-then 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\$2.6 billion and one guarantee of US\$500 million.

The World Bank recently completed a new Systematic Country Diagnostic for Ukraine and is currently preparing a new Country Partnership Framework, which is expected to be approved in 2017.

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 a series of two development policy loans (DPLs), seven new investments, and a guarantee of 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 (DPL -1, US\$750 million approved in 2014, and DPL 2, US\$500 million approved in 2015) and the

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)

Financial Sector (FS) DPL series (FSDPL -1, US\$500 million approved in 2014, and FSDPL-2, US\$500 million approved in 2015).

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 use of scarce public resources effectively 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, power, roads, water and sanitation, health, and social protection.

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 competitiveness of local food producers, help open new markets, and increase access to finance.

Recent Economic Developments

The economy recovered modestly by 2.3% in 2016, with a bumper agriculture harvest leading to stronger growth of 4.8% in the fourth quarter. Decisive reforms in the face of unprecedented shocks in 2014 and 2015 helped to stabilize confidence. As a result, real GDP grew modestly by 2.3% in 2016 after contracting by a cumulative 16% in the previous two years. Signs of stronger growth of 4.8% year-on-year (y-o-y) emerged in the fourth quarter of 2016. The recovery was supported by an abundant harvest, with agriculture growing by 6% in 2016 overall and 18.4% (y-o-y) in the fourth quarter.

Other sectors experienced a pickup from low levels in 2016, with growth of 3.6% in manufacturing, 16.3% in construction, 4% in domestic trade, and 3% in transport. Fixed investment rebounded strongly by 20% from a low base, including manufacturing equipment and imported capital goods, pointing toward strengthened investor confidence. However, the overall pace of recovery remains modest, as significant weaknesses remain in some parts of the services sector, including education, health, and financial services. Stronger recovery has also been held back by weak external demand and the continuing conflict in the eastern part of the country.

After a significant increase in 2015, poverty is estimated to have moderated slightly in 2016. Disposable incomes contracted significantly in 2015 from the deep recession and high inflation. Moderate poverty (applying the World Bank's national methodology for Ukraine) increased from 15% in 2014 to 22% in 2015, while the poverty rate (under US\$5/day in 2005 purchasing power parity, or PPP) increased from 3.3% in 2014 to 5.8% in 2015. In 2016, real household incomes are estimated to have benefited from stabilization in consumer prices and the modest resumption of economic growth. Inflation slowed to 12.4% in 2016 from 43.3% at end-2015 due to exchange rate stabilization and prudent

monetary policy, while real wages increased 11.6% (y-o-y) in December 2016. However, labor market conditions remained weak, with unemployment at 9.9% in the first three quarters of 2016.

The current account deficit widened to 3.8% of GDP in 2016 due to an increase in imports of intermediate and investment goods. Despite a significant reduction of imports of gas and other minerals, the merchandise trade deficit doubled in 2016 due to the increase in intermediate and investment goods imports. Higher foreign direct investment (FDI) inflows—mainly related to bank recapitalization—were sufficient to cover the current account deficit in 2016.

Economic Outlook

The outlook for economic growth remains weak due to the difficult global economic environment, the ongoing uncertainty related to the conflict in the east, and the challenge of advancing reforms on multiple fronts in a complex political environment. Growth is projected at 1% in 2016 and 2% in 2017.

The real depreciation, coupled with reforms to create a level playing field for the private sector, enhance competition, and tap the European Union (EU) market, is expected to support exports and the tradable sectors. Reforms to improve expenditure efficiency should create the fiscal space needed to unlock public investment, while continued reforms in the banking sector should permit a gradual resumption of lending.

The outlook is subject to serious risks, including an escalation of the conflict, further deterioration in the external environment, and difficulty in advancing reforms in the midst of a strained political situation. In light of the gradual economic recovery, poverty is projected to decline only slowly and remain elevated through 2018.

Project Spotlight

The World Bank contributes to the improvement of Ukraine's social assistance system for low-income families through the Social Safety Nets Modernization Project. This Project tackles several key areas: expanding and assisting in financing the Guaranteed Minimum Income (GMI) program, improving the HUS, streamlining oversight and control procedures, continuing administrative modernization, and supporting the deinstitutionalization of children.

Over the past two and a half years, the Project has directly cofinanced the expansion of the GMI program to increase the number of beneficiaries from 200,000 to 300,000 families, which now amounts to over 1 million people. The Project has also supported the implementation of activation services for GMI beneficiaries and internally displaced persons (IDPs) to promote the transition of work-able beneficiaries from benefits to employment. Provision of activation services has started in 2017 as a pilot in three regions; it is expected that 4,000 individuals will benefit from activation measures in these pilots. The national rollout of the activation pilot is planned for 2019.

As part of the Project, most energy-related assistance and privileges have been consolidated into one single program—the HUS. The Project supported an unprecedented scale-up of HUS during the increase in energy tariffs. This massive scale-up from 1 million to almost 6.7 million households by March 1, 2017, managed to cushion the shock of increased prices and facilitate the political acceptability of the new energy prices. This was achieved through a number of major steps to simplify the application process and its administration.

Development of an effective and efficient system to detect, deter, and prevent error and fraud in the social assistance system is another area of assistance. Decreasing the level of spending lost due to error or fraud will reduce the cost of social assistance and positively impact its fiscal sustainability. The Project is supporting the Government of Ukraine in establishing a Social Inspectorate with the capacity to effectively identify and correct benefits irregularities related to error and fraud, and in 2016, the Government began to address the issue by drafting a law to set up this Inspectorate. Starting in 2019, the Government can expect fiscal savings from an improved system of control over error and fraud in the social assistance program ranging from 0.1 to 0.2% of GDP per year.

Progress has also been made in the deinstitutionalization of childcare. The transformation of children's residential institutions and the provision of family-based care to support orphans, children deprived of parental care, children with disabilities, and vulnerable families in the city of Kyiv and Kyiv Oblast (region) have been launched. It is expected that 15 residential institutions in these two regions will be transformed and 2,500 children will be placed in family-based care.

The "Country Snapshot" is a bi-annual update, highlighting the country's recent developments, economic outlook and major overview of the World Bank's partnership with the country. You can find the latest updates at <http://www.worldbank.org/ukraine>



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