



STRATEGY PAPER

November 2016

INTRODUCTION

The Club of Rome, founded almost 50 years ago, has played a significant role in shaping the civilizational thinking of the modern world, especially that of Europe. The publication of *The Limits to Growth* – a famous report to The Club of Rome on the long-term consequences of the global trends of growth in world population, industrialization, food production, resource consumption, and pollution – made a huge contribution to the creation of the modern concept of “**sustainable development**”, which has become a UN strategy.

Europe is the leading champion of the implementation of this vision. The model of “**eco-social market economy**” promoted by major political forces in the EU has become a modern European realization of the sustainable development concept and should serve as a strategic guide for Ukraine. The EU Sustainable Development Strategy officially established this doctrine in the EU and determined the vector of long-term changes of its policy approaches and legislation.

The European Union, despite its current temporary struggles and crises, remains a powerful example for many countries worldwide, particularly with regard to its civilizational values and prospects of sustainable development.

The Agreement on Association and Deep and Comprehensive Free Trade Area between Ukraine and the European Union was finally signed in 2014 and came into force in 2016. This pivotal event has launched the institutionalization of Ukraine’s civilizational choice towards Europe. This choice has been a major factor in the struggle by Ukrainians for independence and “returning Ukraine to where it belongs – the European home” in the period of 1991-2014.

The Ukrainian Association for the Club of Rome believes that adapting the European eco-social market economy model to suit the specific Ukrainian needs in the framework of the European integration process will make a crucial effect on the nation’s competitiveness in the modern age, and should be the keystone in the foundation of Ukraine’s 21st century development strategy.

We believe that today Ukraine is on the verge of major changes, and has a chance to modernize the country in accordance with EU standards and guidelines. There is a growing demand in Ukrainian society, especially among young people, for strategies and policies that would combine political and economic freedom, social justice, and environmental security in a structural and comprehensive way.

UKRAINE’S DEVELOPMENT CHALLENGE

Ukraine has a high potential and exceptional resource wealth: talented and educated people, scientific and technological schools, industrial & transport infrastructure, fertile soil & mineral resources, comfortable climate, unique location between Europe and Asia, etc.

However, Ukraine inherited from the Soviet era an inefficient resource-intensive economy, an extremely neglected environment, as well as the mind-set of an archaic industrial society. And in recent years Ukraine has failed, by its own efforts only, to overcome the adverse legacy of its previous development under communist rule.

Over the past 25 years, the Ukrainian economy has contracted by 35%. According to the World Bank, it is the worst result in the world. Ukraine has lost a third of its real GDP, although in 1990 our GDP per capita (PPP) had a better starting position than Malaysia, Poland and Belarus, and was on the same level as Turkey and Romania.

This unprecedented economic downturn in Ukraine took place amidst large-scale shadowing and monopolization of the economy, technological primitivization of production & exports, de-industrialization, deepening of the financial and foreign energy dependency, flourishing corruption and the formation and preservation of an oligarchic and commodity-based economy. Instead, countries that have introduced the economy of entrepreneurial initiative and innovations, fair market competition and new investment opportunities, economic output and export of products with high added value – have been successfully developing.

Continued policy of market fundamentalism, narrow-minded focus on deregulation and privatization as a panacea, "tightening the population's belts" and fanatical fiscal consolidation along with regular foreign borrowing and restrictive monetary policy of the National Bank of Ukraine have conserved the erroneous economic model in which Ukraine exports raw materials, low-tech products with low added value, talented people and income earned in Ukraine and imports expensive energy, finished products with high added value and international financial aid.

As the result of military aggression of Russia against Ukraine in 2014, and such dysfunctional economic and monetary policy Ukraine has plunged into economic depression, characterized by stable and long-term negative dynamics of GDP, loss of investment, increasing of the debt burden on the budget, the decline in industrial production, exports, employment, household expenditures, the collapse of the Hryvnia exchange rate and inflationary price growth. Instead of creating new prospects for development, the country is on the verge of social destabilization, as millions of people fall below the poverty line, entrepreneurs and the younger generation increasingly migrate abroad in search of a better life. The situation is increasingly becoming even more critical and complicated due to continued military hostilities in Eastern Ukraine.

Comparing the current situation with the real potential, we see a huge gap which can be ascribed, primarily, to a lack of deliberate targeted socio-economic strategy. We need to review the strategy and address the key economic challenges to open up Ukraine's potential to the fullest.

THE WAY FORWARD

Due to its human, natural, infrastructural and other resource potential, Ukraine should be able to bridge this gap through a targeted, holistic and long-term approach, aimed at:

- 1) Sustainable, well-balanced and qualitative economic growth;
- 2) Its socially fair distribution and socially effective use.

MAJOR ECONOMIC AND SOCIAL CHALLENGES

Ukraine faces a number of fundamental social and economic challenges and barriers today:

1. **Low purchasing power.** The dramatic threefold fall of national currency greatly depreciated individual income in Ukraine: average disposable income dropped to \$105 per month. This exhausts the economy and destabilizes the social and political situation in the country.
2. **High unemployment rate.** The official figure is 9.8%, or 1.7 million people, but the real one is even higher than that. Such unemployment rate weakens the economic productivity and additionally depletes the purchasing power of the population.
3. **Lack of investment.** Direct foreign, as well as local private and public, investment is shrinking. Capital investment in future growth (gross fixed capital formation) dropped to 13% of GDP (compared to 20% in the EU and over 25% in developing countries). The annual average outflow of the capital from Ukraine to offshore companies and low-tax jurisdictions is about 8-12 billion USD. The amount of FDI per capita is 5-6 times less than in neighboring EU countries and 12 times less than in the USA.

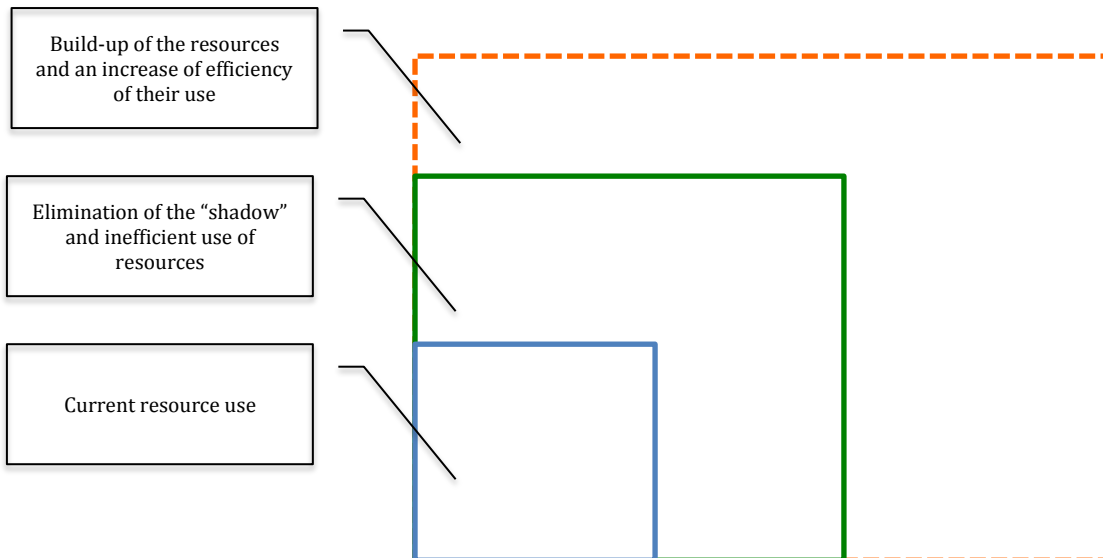
4. **Decline in exports and industrial production.** As a result of military operations in Eastern Ukraine and the loss of the Russian market, as well as the lack of targeted governmental industrial and trade policy, industrial production decreased by 13%, and goods exports fell by 30% in 2015 (despite the effect of EU autonomous trade preferences for Ukraine in the framework of the Association Agreement).
5. **Financial dependence and macro-financial instability.** Mainly due to:
 - a negative trade balance over the past 10 years;
 - threefold devaluation of the national currency;
 - excessive national debt (80% of GDP in 2015; the IMF considers 60% as a critical maximum), and
 - exorbitant national debt interests: 14.3% of public spending in 2016 (the second largest item).
6. **Lack of energy independence and efficiency.** Energy inefficiency in Ukraine is twice as high as in the Czech Republic, 3 times higher than in Poland and 5 times higher than in Singapore. Additionally, Ukraine imports as much as 33% of its energy. This makes many Ukrainian products less competitive on the international market.
7. **Low-tech manufacturing and exports.** A low share of manufacturing in GDP (12% in Ukraine, while being 18% in Turkey and Poland, 21% in Slovakia, and 30% in South Korea), and a miserable share of high-tech exports (only 7% of total exports against 9% in Poland, 15% in the Czech Republic and 47% in Singapore). This leads to a low value added in the economy and, consequently, low social standards in the country.
8. **Excessive shadow economy and social injustice.** The share of shadow economy exceeds 50%. With a total population of over 40 million people, the number of people paying PIT (personal income tax) and pension contributions is only about 9 million. Consequently, the tax burden falls on the shoulders of the least socially protected layers of the population - teachers, doctors, soldiers, and now even working retirees.
9. **Environmental depletion.** For the past 25 years, instead of inclusive realization of human capital, Ukrainian economy has been mainly based on extractive use of exhaustible natural resources, which has led to their significant depletion and deterioration of the ecological situation in the country. The quality of the Ukrainian black soil has gone down as well as of the Ukrainian forestry, etc., and this devastating exploitation of nature has not caused the improvement of social and economic conditions for Ukrainians.
10. **The pervasive corruption and inefficient public service.** Most often, corruption happens in the courts, tax administrations, customs, and other executive authorities. Corruption destroys the trust of the public and business in authorities and puts the brakes on the economy. Public service is too weak and still doesn't address the major socio-economic challenges in a bold, holistic and comprehensive manner.
11. **The loss of human capital.** For 25 years, the death rate has exceeded the birth rate; the number of scientists dropped from 295 000 to 64 000; high emigration: only in the first half of 2015, 411,000 Ukrainians left for work to Poland, which is almost 2.5% of the economically active population; according to surveys, more than 30% of Ukrainians aspire to immigrate to other countries.

OUR APPROACH

Despite the current prevalence of neo-liberal views in the Ukrainian government, we are aware that the aforementioned challenges will not disappear on their own. The fact that the majority of the national establishment still ignores these challenges and continues its laissez-faire policy might result in further worsening of the social and economic situation in Ukraine and might lead to a loss of innovative and sustainable development prospects in Ukraine.

Bold, holistic, comprehensive and long-term strategy aimed at responding to these challenges has no alternative, in our view, if we want Ukraine to fully realize its potential and to use the available resources in the interests of the society:

- Human capital;
- Natural resources (soil, forests, mineral resources, etc.);
- Financial resources;
- Infrastructure.



CONCLUSION

Ukraine's adapting of the European eco-social market economy model to suit the specific Ukrainian needs in the framework of the European integration process is a historic chance for our country to join – as a full-fledged participant – the European and world civilizational processes, and will become a major step forward for Europe as a whole. The successful implementation of the European societal model in Ukraine could have far-reaching and even revolutionary consequences for neighboring countries as well. Bringing Ukraine back into the fold of the European family of nations, with a successful embracing by Ukrainians of democratic governance and a modern innovative and sustainable development strategy, would potentially open new horizons not only for Ukraine, but also for European countries.

The Ukrainian Association for the Club of Rome believes that in the present world Europe and Ukraine desperately need each other. To quote a respected European politician, the former head of the European Commission Romano Prodi, *"Ukraine is important to Europe as a source of economic growth and energy security... On the economic front, Ukraine's 46 million citizens are highly educated, including expert software engineers, skilled industrial workers who power the country's commercial export industries, and capable farmers whose work allows the nation to be the breadbasket of Europe. Indeed, Ukraine's information and high-tech industries can help continue Europe's transformation into the knowledge center of the world... Make no mistake: Western interests and values are best served by engaging Ukraine as a solid European partner. This is a serious geopolitical opportunity for Europe and the US. We should make the most of it."*


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