

Ex-Ante Evaluation (for Japanese ODA Loan)

1. Name of the Program

Country: Ukraine

Program: Economic Reform Development Policy Loan

Loan Agreement: July 17, 2014

Loan Amount: 10,000 million Japanese yen

Borrower: The Cabinet of Ministers of Ukraine

2. Background and Necessity of the Program

(1) Current State and Issues of Ukraine

During 2001-2008, the Ukrainian economy performed well and achieved an average real GDP growth of 7.0 percent, supported by increased capital inflows attracted by the relatively high interest rates. However, the economic growth turned negative in 2009 after the Global Financial Crisis in 2008. The Ukrainian economy returned to positive growth in the following years along with the economic recovery in Europe; despite falling short of the pre-crisis figures, real GDP growth reached 4.2 percent in 2010 and 5.2 percent in 2011. However, as a result of economic slowdown in Russia and in the European Union (EU) member countries caused by the decline in external demand and the fall in natural resource prices, real GDP growth fell to 0.3 percent in 2012, and eventually zero in 2013. The inflation rate dropped to -0.3 percent in 2013 due to a number of factors: inefficient utility prices, de facto fixed exchange rate, a decrease in domestic consumption, and a decline in food prices. De facto fixed exchange rate combined with the fall in external demand led to a decline in exports; in 2013, the current account balance to GDP ratio widened to -9.2 percent, while the fiscal balance to GDP ratio widened to -4.8 percent. Located in between Europe and Russia, Ukraine, whose geopolitical risks especially in the Southeastern region are high, struggled to borrow from the international markets. As a result, its foreign exchange reserves fell below 2 months of imports by February 28, 2014.

The Government of Ukraine has implemented a series of policies to tackle the situation: adoption of floating exchange rate system, introduction of inflation targets, reduction of government expenditures and other policies. However, the abovementioned geopolitical risks pose a threat and the International Monetary Fund (IMF) estimates that the fiscal balance to GDP ratio at -5.2 percent and real GDP growth at -5.0 percent in 2014. The Government of Ukraine needs to confront the challenges to end its economic crisis in the short term; in the medium to long term, build a sound financial condition by improving the governance, business environment and the efficiency of the public sector.

(2) Economic Reform in Ukraine and Priority of the Program

In February 2014, the interim Cabinet, led by the then acting President and Chairman of Verkhovna Rada (Ukrainian Parliament), Oleksandr Turchynov, announced a set of strategies for Ukraine with emphasis on: (1) stabilization of the economy, (2) transparency and anti-corruption, and (3) structural reforms.

Economic Reform Development Policy Loan (the “Program”) supports the economic reforms of the Government of Ukraine by implementing the policy actions. Each policy action, agreed upon by the Government of Ukraine, the World Bank and JICA, is in line with the strategies of Ukraine, contributing to implementation of development strategies.

(3) Japan and JICA’s Policy and Operations in Ukraine

“Building of Mutually Beneficial Economic Relation” is the basic policy of Japan’s Country Assistance Policy for Ukraine (March 2013), whose priority sectors include

“Industrial Promotion for Sustainable Economic Growth.” This Program is in line with the two development issues categorized under the priority sector: “Building of Economic Infrastructure, and Improvement of Energy Efficiency and Environment”; and “Improvement of the Business Environment, and Development of Human Resources.”

Highlights of JICA’s assistance to Ukraine in the past include:

Technical Cooperation: Ukraine-Japan Center (2006-2011)

ODA Loan: Boryspil State International Airport Development Project (2005)

Grant Aid: The Project for Improvement of Medical Equipment for Children's Hospitals (2007)

(4) Activities by Other Donors

On April 30, 2014, the Executive Board of the IMF approved a two-year Stand-By Arrangement (SBA) amounting to US\$ 17.01 billion of which US\$ 3.19 billion was disbursed on May 5, 2014. The World Bank is committed to provide the First Development Policy Loan of US\$ 1 billion; co-financed with JICA, US\$ 750 million was disbursed on May 28 while the remaining US\$ 250 million is scheduled to be disbursed before the end of 2014. The World Bank is also planning to provide the First Programmatic Financial Sector Development Policy Loan amounting to US\$ 500 million before the end of 2014. The EU announced, in March 2014, to provide Macro-Financial Assistance (MFA) amounting to € 1.61 billion as a part of the EU aid package; the first tranche (MFA I) of € 100 million was disbursed on May 20, and the second tranche (MFA II) of € 500 million was disbursed on June 17. In April 2014, the United States announced the support package for Ukraine including the US\$ 1 billion loan guarantee; the National Bank of Ukraine issued a US\$1 billion five-year sovereign bond on May 16. Canada announced, in March 2014, an aid amounting to C\$ 220 million (approximately 20 billion yen), including C\$ 200 million in the form of a loan or a loan guarantee).

(5) Necessity of the Program

By assisting the implementation of economic reform policies, the Program contributes to the efforts of the Government of Ukraine to rebuild financial health and undertake various reforms. Thus, implementation of the Program is highly necessary and relevant.

3. Outline

(1) Program Objective

The objective of the Program is to contribute to the sustainable economic growth of the Ukrainian economy by stabilizing the country economically, through the assistance of the implementation of economic reform policies undertaken by the Government of Ukraine: (1) promote good governance, transparency and accountability in the public sector, (2) strengthen the regulatory framework and reduce costs of doing business, and (3) reform inefficient and inequitable utility subsidies while protecting the poor.

(2) Program Site / Target Area

Throughout Ukraine

(3) Program Components

The purpose of the Program is to provide assistance for the implementation of the economic reform policies by the Government of Ukraine in collaboration with the World Bank. The Program supports the following policy actions, agreed upon by the Government of Ukraine, the World Bank and JICA. The entire loan amount will be disbursed at once as the completion of all the policy actions were confirmed by the end of April 2014.

Pillars	
Policy actions	
1)	Promote good governance, transparency and accountability in the public sector
	1: Enact legislative amendments to reduce exemptions in public procurement from competitive procedures
	2: Government adopts and submits to Parliament legislation to establish centralized external verification of financial disclosures by elected and senior public officials and disciplinary and administrative accountability for those who fail to comply with financial disclosure requirements or misrepresent financial information
2)	Strengthen the regulatory framework and reduce costs of doing business
	3: Enact legislation requiring publication of monthly data on VAT refund processing including claims, refunds, automatic refunds, and arrears; revoke order of the Ministry of Revenue and Duties that establishes targets for additional assessments and fines resulting from audits
	4: Enact legislation to ease business and property registration and reduce the number of permits
	5: Cabinet adopts and submits draft law to Parliament revoking possible use of land as bank capital (State Land Bank)
3)	Reform inefficient and inequitable utility subsidies while protecting the poor
	6: National Energy Regulatory Commission (NERC) adopts resolution to increase residential gas prices by 56 percent (weighted average) and National Commission for Regulation of Communal Services (NCRCS) adopts resolution to increase residential heating tariffs 176 licensees by 40 percent (weighted average)
	7: Cabinet adopts regulation to introduce new targeted program to compensate increase in gas and heating bills of the poorest 30 percent of the population

(4) Estimated Program Cost

10,000 million yen

(5) Schedule

The target period of the Program is from March 2014 to April 2014. The Program will be completed on the day the full amount is disbursed.

(6) Program Implementation Structure

- 1) Borrower: Cabinet of Ministers of Ukraine
- 2) Executing Agency: Ministry of Economic Development and Trade of Ukraine
- 3) Operation and Maintenance System: Not applicable

(7) Environmental and Social Considerations, Poverty Reduction, Social Development

- 1) Environmental and Social Considerations
 - (i) Category: C
 - (ii) Reason for Categorization: The Program is likely to have minimal adverse impact on the environment under the “JICA Guidelines for Environmental and Social Considerations (April 2010).”
- 2) Promotion of Poverty Reduction: None
- 3) Promotion of Social Development (gender issues, measures against AIDS and other infectious diseases, participatory development, consideration for the disabled, etc.): None

(8) Coordination with other donors

The Program is co-financed with the World Bank. The World Bank has disbursed US\$ 750 million of its First Development Policy Loan on May 28, 2014; the remaining US\$ 250 million is scheduled to be disbursed before the end of 2014.

(9) Other Important Issues

The Program is a part of the “Japan’s Assistance to Ukraine” of up to 150 billion yen announced by the Government of Japan on March 24, 2014.

4. Targeted Outcomes

(1) Quantitative Effects

- 1) Performance Indicators:

Pillars	Baseline ^{*1}	Target ^{*1}
Indicators		
1) Promote good governance, transparency and accountability in the public sector		
Share of competitive procurement selection by value (Source: State Statistics Service)	2013: 35%	2015: 55%
Share of new eligible public investment projects appraised and selected through the public investment management system	2013: 0%	2015: 100%
Share of Financial Disclosures Subject to External Verification	2013: 0%	2015: 100%
Coverage of External Audit	2013: State Revenues not included in External Audit (2012 Budget execution)	2016: State Revenues included in External Audit (2015 Budget execution)
2) Strengthen the regulatory framework and reduce costs of doing business		
Ratio of VAT refund claims older than 74 days/quarterly flow of VAT refund claims	2013: 153 percent	20 percent
Number of permits	2013: 143	2015: 84
Distance to the Frontier Doing Business ^{*2}	DB 2014: 58.44%	DB 2016: 66%
3) Reform inefficient and inequitable utility subsidies while protecting the poor		
Fiscal Subsidies to DH companies	2012: UAH 10.4 billion	2015: UAH 0.29 billion
Revenue of Naftogaz from sales of gas to residential consumers	2013: UAH 6.9 billion	2014: UAH 10.4 billion
Number of families below defined income threshold who receive new targeted program	2013: 0	2014: 2 million
Share of means and income tested programs in overall social assistance spending	2012: 13 percent	2015: 20 percent

*1: Unless otherwise noted, both baseline and target values use figures current as of January 1 in the year following the year contained in parentheses.

*2: This measure shows the distance of each economy to the "frontier." The frontier represents the highest performance observed on each of the indicators across all economies measured in Doing Business since the inclusion of the indicator. An economy's distance to frontier is reflected on a scale from 0 to 100, where 0 represents the lowest performance and 100 represents the frontier.

*3: UAH: Ukrainian Hryvnia (1UAH = 11.80JPY as of April 2014)

2) Internal Rates of Return: Not calculated.

(2) Qualitative Effects

Improvement in fiscal situation, governance, business environment, efficiency of the public sector, and others.

5. External Factors and Risk Control

Political and economic situations, especially those in the Southeastern Ukraine, should be closely monitored as they pose potential risks to the Program.

6. Results of Evaluations and Lessons Learned from Past Projects

Ex-post evaluation of the Emergency Budget Support Japanese ODA Loan to the Philippines suggests that the actions by the government of the Philippines on the implementation of various policies – fiscal stimulus and protection of the socially vulnerable in the short-term, and investment in infrastructure for economic growth in the long-term – played an essential role in the economic recovery, with a precise understanding of the country's circumstances and issues, and strong ownership.

Furthermore, the ex-post evaluation of the Energy Sector Restructuring Program for Pakistan by the Asian Development Bank in 2000, points out that one of the important lessons for implementing a program smoothly is to create a close monitoring system between the IMF and the World Bank.

Given the political and economic difficulties, special attention was paid during the discussions on the policy actions so the Government of Ukraine would take full ownership upon the implementations of the agreed policy actions. Specifically, the World Bank and JICA invited not only the executing agency, the Ministry of Economic Development and Trade, but also the Ministry of Finance, the Ministry of Justice, the Ministry of Social Policy and other governmental agencies during the discussions on the policy actions. In addition, considering the financial burden to the citizens, programs to compensate for the increased gas and heating bills were included. Moreover, in close coordination with the World Bank, JICA will monitor the progress of the implementation of the policy actions and the materialization of the outcomes.

Also, given the concerns about the possibility of the policy actions not being implemented as planned by the new Cabinet formed following the presidential election, in March 2014, the IMF mission met each of the presidential candidates to discuss the contents of the economic reform policies. This ensured that the reforms would be consistently implemented regardless of the outcome of the election. Petro Poroshenko won the presidential election on May 25, 2014 with majority of votes; following his inauguration, President Poroshenko continues to implement the policies as did the interim Cabinet.

7. Plan for Future Evaluation

(1) Indicators to Be Used

As outlined in 4. Targeted Outcomes (1) Quantitative Effects 1) Performance Indicators.

(2) Timing

Evaluations will be conducted after the completion of full disbursement of the First Development Policy Loan by the World Bank; specifically, in parallel with the World Bank’s Project Completion Report and the ex-post evaluation scheduled after 2016.