

## REVIEW ARTICLE

# Ukraine's Controversial Transition: How It Became a Market Democracy

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Anders Åslund, *How Ukraine Became a Market Economy and Democracy* (Washington, DC: Petersen Institute of International Economics, March 2009). Pp.248. \$26.95 (paperback) ISBN 978-0-88132-427-3.

Åslund's book represents the only Western volume that seeks to chronicle the last two decades of Ukraine's transition from a Soviet republic in a totalitarian empire with a command administrative economy to an independent democratic state with a market economy. The book is exhaustive in what it surveys but is nevertheless also controversial in the largely positive analysis it gives of the transition process. The volume is also, as I will show, replete with mistakes that devalue its potential contribution to political science, but these could be overcome in future editions.

The book is most excellent when Åslund discusses areas that he was involved in as an adviser to Ukrainian governments. In the early 1990s he describes the 'total confusion in economic policy' and the lack of 'qualified economists'; meanwhile, 'The ignorance of economics as astounding and international interaction was minimal' (pp.30, 44). The lack of understanding of what constituted a market economy during Leonid Kravchuk's presidency during 1991–94 was seen in his economic adviser, Oleksandr Yemelianov, who was, in Åslund's view, the 'most dogmatic communist economist I have ever met' (p.30). In the 1990s Ukraine became an 'oligarchic economy' with insider privatization, state intervention to maximize rents, and corrupt tax and state subsidies (p.128). 'This model of self-reinforcing rent seeking was close to equilibrium and thus stable' (p.128) until the late

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1990s. Åslund blames the above as leading to a 'parasitical rent seeking economy' (p.121), repressed production and a collapse in GDP.

Åslund compares Ukraine's oligarchs favourably to robber barons in the US after the civil war and during Europe's industrial revolution as the only businessmen with local knowledge who could manage the former Soviet plants during the transition to a market economy (p.110). He writes that 'the oligarchs were not guilty of the existing conditions that arose but they responded rationally' (p.112). After 1998, economic and political competition within the elites took Ukraine from its under-reform trap, and the privatization of large plants led to transformation of oligarchic commodity traders into industrialists by giving the oligarchs autonomy from the state (p.123). Much of this process of transition from oligarch to capitalist Åslund credits to the Viktor Yushchenko government of 1999–2001 which legislated reforms, reduced energy corruption, and cleaned up the state budget.

Åslund credits Kuchma with launching a successful programme of privatization in 1994 that allegedly transferred the majority of Ukraine's GDP to the private sector within two years, leading to the emergence of a market economy by 2000 (Ukraine was recognized as a 'market economy' by the US and EU only in 2005–6). These optimistic figures are contradicted by Åslund citing EBRD figures that Ukraine's private sector accounted for 65 per cent of the country's GDP by 2002 (Åslund believes the true figure to be already 80 per cent). Was a majority of Ukraine's GDP in the private sector by 1996 or 2002?

Åslund credits the Yushchenko government with making Ukraine's market economy irreversible and Kuchma with establishing a reform team 'that was to last' drawing upon 'nationalist liberal economists', such as Viktor Pynzenyk and Yushchenko, with Yuriy Yekhanurov Ukraine's answer to Russia's Anatolii Chubais; that is, those political forces who supported the 2004 Orange Revolution (p.45). Yekhanurov 'secured the success of Ukraine's privatization' in 1994–97, but only after 2000 did privatized companies become more efficient than state ones (p.80). 'In the end privatization worked', Åslund proclaims (p.81). Because Ukraine began the process of privatization later than Russia it reached Russia's level, according to Åslund, only in 2005, 'when Russia reverted to renationalization' (p.81).

Kuchma's 1994 programme, according to Åslund, went further than Yegor Gaidar's in Russia two years earlier, and was similar to Poland's 'Balcerowycz plan'. What let Ukraine down was the fact that following the IMF-backed stabilization there were no liberal or fiscal reforms, thereby dragging the transition on longer – until 2000, when Ukraine finally established a market economy. Kuchma's deregulation of November 1994 'marked Ukraine's decisive transition to a market economy' and 'Kuchma exceeded all expectations with this reform' (p.75). After the adoption of the semi-presidential

Constitution in 1996, Kuchma ‘lost interest’ in further reforms and under the next three prime ministers (Yevhen Marchuk, the notorious Pavlo Lazarenko, who now sits in a Californian jail, and Valeriy Pustovoytenko) Ukraine returned to a ‘state-regulated transition to a social-market economy’ (pp.86–7).

Ukraine’s reforms were not undertaken with public and parliamentary backing. ‘The public neither understood nor believed in a market economy’, Åslund notes (p.88), while ‘capitalist ideology was too weak’ (p.88). Kuchma himself wavered, and he ‘was no visionary, but a deadpan realist’ (p.90). Parliament, led by the left from 1994 to 1999, was largely opposed to economic reforms, while former communists-turned-centrists lacked any ideology and the old *apparat* was ‘counter-revolutionary’ (p.88).

Yushchenko’s government was a breath of fresh air and was backed by a large coalition of ten centrist and national democratic factions who had taken control of parliament. The former National Bank chairman Yushchenko was not tainted by corruption and was allegedly a ‘Ukrainian nationalist’ (p.132), a disputable assertion. The government brought together a team of reformers, including Yulia Tymoshenko, who ‘were more experienced and knowledgeable than in 1994 and ready to play hardball’ (p.133). The first four months of 2000 ‘saw the greatest reform drive that Ukraine had seen since the autumn of 1994. It was broader and more comprehensive, and it would put the market economy right’ (p.133). The Yushchenko–Tymoshenko administration focused on central government reforms, fiscal reform, reform of the corrupt energy sector, land reform, privatization of large industrial plants and Ukraine’s first successes against corruption. Tymoshenko cleaned up the energy sector by removing \$4 billion annual rents (accounting for 13 per cent of GDP) going to oligarchs by ‘enhancing transparency and eliminating barter’ (p.138–9), which led to greater payment discipline and higher tax revenues.

Åslund touches too briefly on one of the many negative side effects of the transition: organized crime and corruption. Crime in the 1990s ‘became unbearable’, he admits, in a rare criticism of the era and during the Lazarenko government of 1996–97; Åslund argues: ‘organized crime appeared to have taken power’ (p.113). In 2000, oligarchs allegedly took over organized crime during their transition from oligarchs to capitalists. Åslund credits the Yushchenko government with significantly reducing rent seeking by inviting Tymoshenko to join the government, where she went about ‘diminishing the oligarchs’ energy rents’ (p.148).

Åslund’s analysis becomes controversial – and questionable – when he attaches blame to events during the transition. He blames Ukraine’s evolutionary reforms for ‘severe corruption and rent seeking’ (p.55) without explaining why these two phenomena were still present in Russia which opted for shock therapy. Åslund is under the misapprehension that because Russia undertook market reforms earlier it therefore ‘limited its social costs of transition’ (p.2),

an assertion that is highly debatable. Allegedly, 'Ukrainians were prepared to accept higher social costs because their project was to build a nation' (p.2). Ukraine, in Åslund's view, suffered more social costs, 'social suffering and sharply rising income differentials' (p.56). Åslund provides no proof to back up this radical claim that Russia suffered fewer social costs than Ukraine because it undertook shock therapy.

Åslund's view of government is that it should be minimalist, and he castigates Ukraine's allegedly high public expenditure as a share of official GDP, which declined from 44 to 34.5 per cent in the late 1990s, a figure that he defines as still too high (p.136). When compared with North American and European democracies this figure seems perfectly reasonable: the figure for the US before the 2008 global financial crisis was 36 per cent, that for Canada and Germany 48, Scandinavian countries averaged over 50, Britain was 50, and France 60 per cent. What measure does Åslund therefore use to claim that Ukraine's 34.5 per cent of GDP spent by the government was still 'too high'? Measured against established market economies it was too low.

Åslund's discussion of the Orange Revolution is convoluted and subjective, ignoring areas that he does not wish to see. Ukrainians protested for three broad reasons: the trigger was massive electoral fraud and resultant fear over the democratic or authoritarian course of the country. However, these factors alone would never have brought one in five Ukrainians on to the streets. Two other factors – that Åslund ignores – were the facilitators of the protests: social issues (including anti-elite sentiments, disgust with corruption, anger at 'oligarchs' and support for the slogan 'Bandits to prison') and national identity (the majority of protesters were Ukrainophones from western and central Ukraine). Åslund is right to say that Yushchenko played down his 'ethno-nationalism' in the 2004 elections, standing instead as a centrist and conservative candidate on a platform of good governance, private property and European integration (p.179). In reality, however, Yushchenko's 2004 programme never mentioned NATO or the EU (Åslund does admit that Yushchenko's programme barely mentioned foreign policy (p.187)). Yushchenko's election campaign of 2010, in contrast, regressed to anti-Russian, Galician nationalism.

Åslund's lack of understanding of the social forces behind the Orange Revolution is surprising in the light of his claim that Yushchenko 'focussed on universal values, notably freedom and legal justice, directed against oligarchic repression and corruption' (p.179). He briefly refers to the slogan repeatedly raised by Yushchenko of 'Bandits to prison' but says that he presumably did not really mean it since he 'also promised a peaceful transfer of power and no revision of privatization' (p.187). Allegedly, 'Populist or economic slogans were absent' from Yushchenko's 2004 programme

(p.187). Åslund sees what he wishes to see rather than analysing the facts, as any reading of Yushchenko's 2004 programme and 14 draft decrees ready to be signed after he took power will show that they were heavily social-populist, and after his election Yushchenko gave the state property fund to the Socialist Party which opposed privatization. Tymoshenko took Yushchenko's 2004 programme as the basis of her 2005 and 2007–8 government programmes. Åslund ignores this fact, claiming that Yushchenko was not a populist in 2004, and supports Yushchenko's criticism of the 2005 Tymoshenko government as 'populist' and obsessed with reprivatization (pp.202, 205) although it sought to implement Yushchenko's election programme. A disconnect between reality and fiction is evident when Åslund argues (p.207) that '[Tymoshenko's] policy was almost exactly the opposite of the liberal Yushchenko', making this reader wonder whether Åslund has actually sought to study Yushchenko's 2004 programme and draft decrees. Åslund laments Tymoshenko's economic policy as a 'disaster' because 'businessmen were upset by her populist economic policy' (p.208), an argument that again reveals his positive inclination towards oligarchs and disregard for the popularity of her social welfare and anti-oligarch policies among ordinary Ukrainians. The irony of ironies is that Yushchenko's election campaign in 2010 claimed credit for much in the government's social policies that he had earlier condemned as 'populist'.

Åslund's discussion of the last four years of the Yushchenko era is interesting for its insights but problematic in its mistakes. His discussion of the post-2006 election negotiations is interesting for the insight it reveals into how Yushchenko was indecisive over supporting a grand coalition between Our Ukraine and the Party of Regions or an orange coalition between Our Ukraine and the Socialist Party and Tymoshenko bloc (BYuT) (p.215). In September 2006, Viktor Baloga took over as head of the presidential secretariat and remained in the post until his resignation in May 2009, the longest-serving of four chiefs-of-staff. Åslund describes Baloga as 'a crisis manager and fighter with no apparent ideology' who removed from the secretariat 'all liberals and orange revolutionaries' (p.217). If this insight is correct it reveals the extent to which Yushchenko's presidency was already in stagnation by his second year in office, after suffering an earlier crisis in September 2005 when he dismissed the Tymoshenko government.

Åslund changes his position towards the second Tymoshenko government in 2007–9, claiming that it was no longer 'populist', a highly misused word that Ukrainian politicians and Western analysts of Ukrainian politics throw around like confetti at a wedding without any inkling of its meaning in political science. Åslund has a warmer attitude to the second Tymoshenko government because it no longer supports reprivatization, supports a market economy and Ukraine's membership of the World Trade Organization (WTO) and has

new oligarch allies. Much of this, contrary to Åslund's claim, did not suddenly appear in 2007. As he himself points out, the oligarchs and 'minigarchs' (meaning billionaires and millionaires) supported both Yushchenko and Yanukovych in the 2004 elections, BYuT was always supportive of a social-market economy (as are most Ukrainian parties, including Our Ukraine) and the first Tymoshenko government and BYuT voted for legislation required to join the WTO. The only factor that changed between 2005 and after 2007 was the removal of reprivatization from the government's agenda, the main issue that was Åslund's bugbear.

Åslund's analysis of Ukrainian politics in 2008–9 is highly critical of Yushchenko, who he says 'never gave Tymoshenko a chance to govern and he achieved a complete government stalemate' (p.222). From April 2008 Yushchenko vetoed everything the government did, prohibited governors from meeting the prime minister, halted privatization, while 'Yushchenko spoke like an old-style socialist...' (p.223). Åslund outlines the president's three objectives that led to political instability: break-up of the coalition that he had campaigned for in the 2007 elections, removal of the Tymoshenko government in which he had demanded Our Ukraine receive half of the ministerial positions, and provoke pre-term elections (p.231). Yushchenko 'seemed obsessed with Tymoshenko, speaking and acting as if his only endeavour was to destroy her' (p.231). This was clearly seen in Yushchenko's 2010 election campaign which was based on daily falsehoods, claims and attacks on Tymoshenko who was accused of being the cause of every problem in the country.

Åslund is certainly correct to argue that 'Yushchenko seems to have burned the last of his capital of trust in 2008' (p.231), as his popularity steadily declined throughout the year to single digits. Nevertheless, 'Yushchenko's behavior in 2008 was perplexing. Although he formed a coalition with Tymoshenko, he never gave her government a chance to work' (p.232). This paradox cannot be explained by political science; the explanation lies more in the realm of Yushchenko's psychology and possibly his attitude to Tymoshenko in terms of gender politics and relations.

In December 2004, Yushchenko negotiated a compromise package at three round-table meetings that included a change to a new constitution two years later that reduced his powers (p.196). All parliamentary forces, including Our Ukraine, voted for the package: the only political force to oppose the constitutional changes was BYuT. Åslund argues that the best political system for Ukraine would be parliamentarism and that therefore the 2006 constitutional changes did not go far enough. Post-communist East European states that have become democracies and EU members have adopted parliamentary systems, which points to a link between parliamentarism and democratization. Post-communist states in the Commonwealth of Independent states (CIS), with

the exception of only Ukraine and Moldova, have adopted presidential systems and have autocratic political systems. Parliamentarism is best suited to support Ukraine's integration into Europe. At the same time, five years of political instability under Yushchenko have produced a broad consensus on the 'failure' of parliamentarism, with strong support among all presidential candidates in the 2010 elections for a return to a presidential system.

The next edition of Åslund's book should study Ukrainian opinion polls to see how Ukrainians have low trust in state institutions, with the exception of 2005 immediately following the Orange Revolution when public trust was high. It is not therefore the case, as Åslund argues, that Ukraine's political institutions and economy 'were considered highly legitimate' (p.258) and that the market economy 'enjoys solid political support' (p.259), two claims that reflect Åslund's wishful thinking rather than Ukrainian reality as seen in sociological surveys. A survey of post-communist countries by Pew Associates in November 2009 found that Ukrainians had one of the lowest supports for the transition to a market economy.<sup>1</sup> Only 36 per cent of Ukrainians approve of their country's transition to capitalism and only 30 per cent approve of the democratic changes (Russia was higher in both categories).

The next edition of Åslund's book will require the correction of a large number of mistakes. Kravchuk never gave up nuclear weapons 'too cheaply' (p.41) – this was Kuchma in 2004–6. It was likewise not Kravchuk but Kuchma who instigated Ukraine's de-nuclearization and provision of security assurances (not 'guarantees' as Åslund wrongly describes them (p.58)). Åslund inter-changes use of 'assurances' and 'guarantees' (p.228) which are two very different propositions. Åslund alleges that the US 'has amply guaranteed Ukraine's security through the US–Russia–Ukrainian declaration of January 14, 1994 and the START treaty' (p.264), an assertion that is not supported by evidence from Ukrainian leaders and specialists who argue that the Budapest Memorandum<sup>2</sup> is worthless and who fear the implications for Ukrainian security of the Obama administration's re-setting of its relations with Russia.

Åslund alleges that the Ukrainian public rewarded Kuchma 'with persistent support in public opinion polls' (p.91), which was not the case, as seen in his less than 10 per cent support on the eve of the 1999 elections. Åslund sincerely believes that Ukrainians supported and welcomed the transition to a market economy and thanked Kuchma accordingly, a dubious claim that is not backed by any sociological surveys. In the 1990s, 'Corruption did not abate but probably grew worse' (p.91), argues Åslund in an off-handed manner, at a time when corruption became widespread and a small coterie of loyalist oligarchs became super-wealthy. The security service (SBU) is described as an organization with 'only' 28,000 officers (p.113), which is very large compared with the combined membership of Britain's MI5 and

SIS (MI6) of 6,000. Åslund's comparison of Ukraine's oligarchs to American robber barons in the nineteenth century does not stand up to analytical scrutiny: two centuries ago there were no offshore banking facilities, and capital, although often illegally earned, stayed at home. Åslund's description of Yushchenko as a 'nationalist' (p.132) is misleading as it confuses centre-right national democrats with the extreme right.

Åslund writes that 'The roles of Kuchma and his chief of staff Volodymyr Lytvyn in this drama [Kuchmagate] remain unclear' (p.144).<sup>3</sup> Their roles have been thoroughly studied in Ukraine and by Western scholars who have analysed the background to the murder of opposition journalist Heorhiy Gongadze. Åslund's discussion of the despatch of Interior Ministry (MVS) special forces to Kyiv on 28 November 2004 is confusing and seeks, as with the Gongadze murder case, to remove any association of violence with Kuchma (p.195). As the incumbent president Kuchma was constitutionally responsible for ordering violence to be undertaken against opposition journalists, for permitting massive election fraud in 2004 and for transferring MVS special forces to Kyiv.

Åslund praises the 2006–7 government of Yuriy Yekhanurov for two reasons: he credits him first with securing privatization (p.81) in the 1990s when he was head of the State Property Fund, and secondly with replacing the 'populist' Tymoshenko government and re-establishing warm relations with the 'national bourgeoisie' (Yekhanurov's depiction of oligarchs). The Yekhanurov government is culpable in negotiating a poor gas contract in January 2006 that introduced the corrupt gas intermediary RosUkrEnergO which did the most to corrupt Ukrainian politics and the Yushchenko presidency.<sup>4</sup>

Åslund is highly critical of Ukraine's non-adoption of shock therapy policies, believing that this delayed the transition to a market economy. He wrongly believes that among post-communist countries Ukraine's evolutionary transition to a market economy was an exception (p.237), ignoring the large number of delayed and slow reformers in Eastern Europe such as Serbia, Croatia, Slovakia, Romania and Bulgaria. Åslund wrongly therefore argues that most East European countries 'were radical reformers and quickly became democracies' (p.237), ignoring the fact that the former communist old guard ran Bulgaria, Slovakia and Romania until the second half of the 1990s.

Åslund's discussion of Ukrainian foreign policy is one of the weakest parts of the book. He argues simplistically that Ukraine will inevitably turn to the West as 'Russia does not offer anything' (p.238) – a view that ignores Ukraine's dilemma of being offered NATO but not EU membership. Ukrainians support EU membership which is currently not on offer, but oppose NATO membership which was on offer but is now on a back burner owing

to Ukraine-fatigue in NATO and the EU and a change in US policy as the country replaced President George W. Bush with President Barack Obama. Besides NATO's bombing of Yugoslavia in 1999 (p.226), the US-led coalition invasion of Iraq in 2003 also damaged Ukrainian public sentiment regarding NATO membership, as Ukrainians associate the US with NATO, as did the anti-NATO and anti-American Yanukovich 2004 election campaign.

## NOTES

1. 'End of Communism Cheered but Now with More Reservations. The Pulse of Europe 2009: 20 Years After the Fall of the Berlin Wall', Pew Research Center, 2 Nov. 2009, available at <<http://pewglobal.org/reports/display.php?ReportID=267>>, accessed 14 Feb. 2010.
2. A meeting in Budapest on 5 December 1994 adopted a memorandum on security assurances to Ukraine, as the country prepared to accede to the nuclear non-proliferation treaty. According to the terms of the memorandum, the USA, the Russian Federation and the UK undertook to respect Ukraine's borders, to refrain from the use or threat of use of force against Ukraine, to refrain also from economic coercion against the country, and to bring to the United Nations Security Council any act of nuclear aggression against Ukraine.
3. 'Kuchmagate' refers to the case of the discovery of the headless body of a Ukrainian journalist, Heorhiy Gongadze, in November 2000, and the subsequent unveiling of a tape recording by presidential guard Mykola Melnychenko purportedly linking his abduction and death to President Leonid Kuchma.
4. 'It's a Gas: Funny Business in the Turkmen-Ukraine Gas Trade', *Global Witness*, 25 July 2006, available at <[http://www.globalwitness.org/media\\_library\\_detail.php/479/en/its\\_a\\_gas\\_funny\\_business\\_in\\_the\\_turkmen\\_ukraine\\_g](http://www.globalwitness.org/media_library_detail.php/479/en/its_a_gas_funny_business_in_the_turkmen_ukraine_g)>, accessed 14 Feb. 2010.