
Economic Constraint and Ukraine's Security Policy



Dominic Fean

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- “Ianoukovitch et la politique étrangère ukrainienne : retour à l'équilibre ?” *Politique Etrangère*, No. 2, 2010;
- “Making Good Use of the EU in Georgia: the ‘Eastern Partnership’ and Conflict Policy,” *Russie.Nei.Visions*, No. 44, September 2009.

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Introduction

Ukrainian security policy is often analyzed through the prism of Kyiv's relations with Moscow. Since independence, Ukraine's international orientation has been closely tied to the debate over whether the future of the country is tied to its relations with Russia or with the West, most often identified as the North Atlantic Treaty Organization (NATO) or the European Union (EU). Discussion of political orientation, however, often serves to obscure the true driver of Ukraine's choices in foreign and security policy: economic interests.

Since winning Ukraine's 2010 presidential elections, Viktor Yanukovich has tried to repair much of the damage caused by a precipitous decline in the relationship between Kyiv and Moscow under his predecessor Viktor Yushchenko (2005-2010). After the Orange Revolution, issues like the role of the Russian language in Ukraine, Ukraine's steps toward NATO membership, the 2008 war in Georgia and bilateral gas relations caused acrimony on both sides.¹ The incentives for Yanukovich's efforts have been at least partly political. Russia has always played an important role in Ukraine's domestic politics, questions of Russian identity being a source of internal division.

While Viktor Yushchenko had set NATO membership as a priority, Viktor Yanukovich has made refusal to join military alliances one of the cornerstones of his foreign policy position. The law "On the Principles of Domestic and Foreign Policy" states that: "as a non-bloc European state, Ukraine follows an independent, open foreign policy and hopes to cooperate with any interested partner, whilst avoiding dependence upon certain states, groups of states or international structures. [...]eaning the non-participation of Ukraine in political and military alliances."² Seen as a concession to Russian objections to NATO enlargement, it could be interpreted as evidence that Yanukovich is subordinating Ukraine to Russian interests. However, cooperation with NATO continues apace and the new government has not called into question the reform program intended to prepare the military for membership.

Under Yanukovich, security questions have become increasingly entwined with economic concerns. A Russo-Ukrainian agreement signed in April 2010 in Kharkiv formalized a price discount for Ukraine on Russian gas supplies to 2019. An agreement extending Russia's lease on naval facilities in Crimea was signed concurrently (see textbox 1). Signature of

¹ See D. Medvedev, "Address to the President of Ukraine Viktor Yushchenko," 11 August 2009, <<http://archive.kremlin.ru/eng/text/docs/2009/08/220759.shtml>>.

² Ukrainian National Information Agency, "Zakon Ukrainy 'Ob osnovakh vnutrenney i vneshnej politiki'" [Ukraine's Law "On the Principles of Domestic and Foreign Policy"], No. 2411-VI, 1 July 2010, <www.ukrinform.ua/rus/order/?id=943396>.

*Textbox 1: Kharkiv Agreements,
21 April 2010*

For the duration of the 2009 ten year gas contract, Ukraine is to receive a discount of 30% on the base price. When gas prices under the 2009 pricing formula exceed US\$ 330/tcm, this discount is capped at US\$ 100/tcm. From 2011, the discount applies to the first 40bcm of the 52bcm/y contracted under the 2009 agreement.

The reduction takes the form of a discount on export duties charged by the Russian Federal government; as a result it only affects the Federal budget's balance sheet and not Gazprom's—underlining the political rather than economic nature of the reduction. The reduction needs to be approved by the Russian Parliament on an annual basis.

This concession in the gas trade is seen as a direct exchange for the extension of basing rights for Russia's Black Sea Fleet (BSF) on Ukraine's Crimea peninsula, which was signed simultaneously. The lease was signed for a further 25 years, meaning that the Russian navy will stay in Sevastopol until at least 2042.

these accords has caused controversy in Ukraine, and abroad, since it is seen as the trading of Ukrainian sovereignty for short term financial benefits. One analyst described the deal as amounting to “a mortgaging of some of Ukraine's independence”.³

Gas supply has long been a problem in Ukraine's relationship with Russia, its main gas supplier. Disputes over gas pricing and transit rights led to supply cuts to Ukraine and Europe in 2006 and 2009, the yearly renewal of contracts was a source of tension, which was finally brought to an end by the signing of a ten-year contract in January 2009. The resolution to the 2009 dispute negotiated by the Prime Ministers of Russia and Ukraine, Vladimir Putin and Yulia Tymoshenko, led to

expectations that the bilateral gas trade might finally become more stable.⁴

The Kharkiv agreements have thus opened the door to greater Russian influence in the future and guaranteed Russia's military presence in Crimea for a considerable time to come. The ability to use this foothold to exert pressure on Ukraine as a whole is well understood in Russia.⁵

While the effects of these agreements are both political and economic, their motivation is almost entirely the latter: Yanukovich's rapprochement with Russia is calculated to extract the maximum financial benefits possible. The Ukrainian industrial elite rely heavily upon ties with Russia, particularly in the energy sector. After a disastrous 2009, during which Gross Domestic Product (GDP) declined by nearly 15%, Yanukovich has worked hard to revitalize the Ukrainian economy, working with both Russia and the International Monetary Fund (IMF) on possible ways to reduce the budget deficit.

In spring 2011, Yanukovich is expected to sign into law a new defense doctrine, already approved in draft by the Rada, Ukraine's parliament. It will most likely reinforce the steps already taken away from NATO membership track while reinforcing pre-existing reform plans. While

³ J. Sherr, “The Mortgaging of Ukraine's Independence,” Chatham House, Briefing Paper, REP BP 2010/01, August 2010, p. 3.

⁴ S. Pirani, J. Stern, and K. Yafimava, “The Russo-Ukrainian Gas Dispute of January 2009: A Comprehensive Assessment,” Oxford Institute for Energy Studies, NG 27, February 2009.

⁵ M. Barabanov, “Russia's Black Sea Fleet Deal with Ukraine—the Political Aspects,” *Moscow Defense Brief*, No. 2, 2010, p. 8-10.

the wider geopolitical positioning appears to be orienting Ukraine more towards Russia, the Kharkiv agreements underline the ever closer integration of the defense and economic fields in Ukraine. This is an important factor to consider, while defense questions naturally have to be decided within the confines of economic resources, the Yanukovich government is progressively subordinating strategic issues to the economic interests of the country and its ruling classes.

In order to explain these developments, this paper will first examine the domestic conditions encouraging Ukraine's return to more cordial relations with Russia. While for reasons of domestic harmony relations with Russia are important, they are also vital to Ukraine's economic wellbeing and that of the ruling elite. Secondly, the recent history of Ukraine's armed forces reform will be addressed, finding that economic constraint has long been a reality, and even proponents of NATO membership have failed to supply the funding necessary for effective reforms. Finally, the reasoning behind a relative rapprochement with Russia is examined, with care taken to separate the motive and effects of recent developments. Taking these elements into account, the paper concludes that while the Russian-Ukrainian relationship is important in Ukrainian political debate, economic and budgetary concerns play a predominant role in Ukraine's security policy. Yanukovich may have some attachment to friendly relations between Russia and Ukraine, yet his motivations do not lie in this area.

Domestic Interests in Rapprochement with Russia

Given the speed with which Yanukovych moved to repair relations with Russia, and the manner in which this was done, it could be argued that good relations with Ukraine's eastern neighbor are something of an ideological objective of the president. As this section argues, relations with Russia are important for Ukrainian politics—particularly the cultural identities of the different regions of Ukraine; however, there are more tangible and pressing reasons for the Ukrainian government to pursue ties to its counterpart in Russia.

Russia in Ukraine's domestic politics

Ukrainian society is deeply divided on the question of identity. Many Ukrainians have ethnic Russian heritage and speak Russian as their mother tongue, causing tensions with a more nationalist Ukrainian speaking section of the population who are suspicious of Russia and its role in suppressing Ukrainian culture under the Russian empire and Soviet Union. As such, the question of Ukraine's relationship with Russia is not just a foreign policy issue, it fuels domestic debates on identity and the orientation of the country especially since Ukraine has had difficulties establishing its independence vis-à-vis its former colonial master.

The vehemence with which the debate is pursued can be seen in the controversy over the awarding (by Yushchenko) of the title of Hero of Ukraine to Stepan Bandera—a World War Two era anti-Soviet fighter who allied himself with the Nazis.⁶ On the other side of the debate, the Rada ratification of the Kharkiv accords was accompanied by a brawl and many objected that the extension of basing rights contravened the Ukrainian Constitution, which stipulates that “location of foreign military bases shall not be permitted on the territory of Ukraine.”⁷

Yanukovych is a particularly divisive figure in this context given the perception that he was “Russia's man” in the 2004 presidential elections that preceded the Orange Revolution. In addition, his electoral base is focused upon regions in the east of Ukraine, where sympathies toward Russia are seen as strongest.

⁶ D. Fean, “Ianoukovitch et la politique étrangère ukrainienne : retour à l'équilibre ?” *Politique Etrangère*, No. 2, 2010, p. 425.

⁷ Article 17, Constitution of Ukraine.

These debates have a security angle too. Ukrainian analysts maintain that a lack of national unity is a problem for the security of the state. They also highlight that while it may be independent, “[a]t present, Ukraine is neither economically, politically nor culturally autonomous.”⁸ It is this lack of autonomy which conditions the domestic pressures which encouraged Yanukovych to pursue cooperation with Russia.

Yanukovych, the ruling class and gas interests

Despite the importance of relations with Russia for the domestic political scene, the subjugation of national interests to the business interests of the ruling elite is more important to our understanding of the Kharkiv accords. Oligarchs—many of whom have entered politics—exert a strong influence on political life through their financial clout, media ownership and the dependence of politicians upon their financial backing. This situation emerged under the presidency of Leonid Kuchma (1994-2005), but was left unchallenged by the reformers that came to power after the Orange Revolution.⁹ As a result, fortunes have been made through access to administrative resources and government contracts, not as a return on investment or the development of efficient industry.¹⁰

Leading figures in Yanukovych's Party of Regions of Ukraine (PRU) have business interests that are especially dependent upon gas imported from Russia. As the owner of Ukraine's largest steel producer, Metinvest, Rinat Akhmetov—Ukraine's richest businessman, Rada member and backer of the PRU—has substantial interest in the price of gas due to the importance of energy supplies to steel production. A strong contingent within Yanukovych's team has links to the gas industry, and most particularly to Dmytro Firtash: a Ukrainian businessman who made his fortune in the gas trade and has large interests in the gas-intensive fertilizer sector. Not least among them is Yuri Boyko, the Minister of Fuels and Energy who previously worked for Dmytro Firtash as a manager of RusUkrEnergo, the gas trader deeply embroiled in suspicious gas exchanges with Russia. Sergey Lyovochkin, the head of the Presidential Administration under Yanukovych also has ties to Firtash. The prominence of these figures within the ruling elite is seen as a victory for the interests of the oligarchs linked to the gas trade.¹¹

The rise of the Gas-group in Yanukovych's ruling circle also accounts for the determination of the president to reduce the prices of gas imports. This is particularly the case in the context of Ukraine's drawn-out

⁸ V.P. Horbulin, O.F. Byelov, and O.V. Lytvynenko, *Ukraine's National Security: An Agenda for the Security Sector*, Zurich, Geneva Center for the Democratic Control of Armed Forces, 2010, p. 43-44.

⁹ E. Chow and J. Elkind “Where East Meets West: European Gas and Ukrainian Reality,” *Washington Quarterly*, Vol. 32, No. 1, 2009, p. 85-86.

¹⁰ R. Puglisi, “The Rise of Ukrainian Oligarchs,” *Democratization*, Vol. 10, No. 3, Autumn 2003, p. 104.

¹¹ D. Fean, *op. cit.* [6], p. 423-424.

economic crisis, which has severely damaged the capacity for Ukrainian businesses to compete with foreign rivals.

Financial crisis

The financial crisis of 2008-2009 greatly affected Ukraine's political landscape. The Kharkiv accords illustrate the effects of the crisis in encouraging the convergence of security and economic interests at a time of exceptional uncertainty for the Ukrainian state.

Ukraine's gross domestic product began to drop in the final quarter of 2008 and fell 14.8% year-on-year in 2009; industrial output fell 21.9% in the same period.¹² With presidential elections expected in early 2010, no political force was willing to make the painful decisions necessary to address the economic imbalances in Ukraine. In order to stave off national default, the International Monetary Fund (IMF) prepared one of its largest programs to date, establishing a Standby Arrangement of Standard Drawing Rights valued at 16.4 billion US dollars.

The crisis hit the banking sector hard, requiring substantial recapitalization by the state. An unsustainable and unreformed state pension system was also a major drain on government finances, but the cost of Ukraine's gas supply was a predominant risk factor.

Unofficial subsidies paid to Naftogaz Ukraine, the state gas monopoly as one of the main burdens on the budget—representing 2.7% of GDP in 2009.¹³ The Ukrainian state consistently covers Naftogaz's debts despite its functional deficits due to household and industrial gas tariffs that do not reach cost recovery levels and a lack of payment discipline on the part of municipal heating companies. While overall gas consumption did fall in 2009, it did so in the relatively profitable industrial sector, which cut production due to the decline of steel and chemical markets worldwide, further exacerbating Naftogaz's financial situation.¹⁴

Ukraine was unable to meet its commitment to the IMF to deliver a balanced budget in 2009, its initial stance was to have a deficit of 8.6% of GDP (including 2.6% of GDP to cover Naftogaz's debts). However, political maneuvers in the run up to the presidential elections left Ukraine at loggerheads with the IMF, which suspended its assistance until after the

¹² EBRD, "Transition Region: Quarterly GDP Actuals and Projections, Q2 2008- Q4 2010," last consulted 28 January 2011. Available at: <www.ebrd.com/pages/research/economics/data/macro.shtml#macro>; S. Pirani, J. Stern, and K. Yafimava, "The April 2010 Russo-Ukrainian Gas Agreement and its Implications for Europe," Oxford Institute for Energy Studies, NG 42, June 2010, p. 33.

¹³ IMF, "Ukraine: Second Review Under the Stand-By Arrangement and Request for Modification of Performance Criteria—Staff Report," *IMF Country Report*, No. 09/270, September 2009, p. 18.

¹⁴ Interview with EBRD specialist, June 2010.

polls. In the event, Ukraine built up a deficit of 11.4% of GDP for the whole year.¹⁵

Thus in addition to the desire to repair relations with Russia, the Gas-for-Fleet deal represented a means for Ukraine's government to secure international loans. Conscious that the IMF program was on hold until Kyiv demonstrated greater commitment to reducing the budget deficit, Yanukovych wanted to alleviate the strain of Naftogaz upon state finances as a step toward securing additional IMF funds. This reconfirms the subordination of strategic to economic concerns, but challenges the importance of the Russian vector: it was not just Russian money that was to be gained from the Kharkiv deals, but IMF funds also.¹⁶

The Kharkiv agreements increased the likelihood of renewed IMF lending

It is important to note that resolution of the deficit problem by reducing the cost of gas would improve the profitability of Ukrainian industries, but could delay the reform of Naftogaz. Experts note reluctance to inject transparency into the Ukrainian gas sector, believing that lack of clarity is in the interest of corrupt Ukrainian officials.¹⁷ Despite incremental rises in energy tariffs bringing households closer to cost-recovery level, the longer the Ukrainian government delays reform, the longer Naftogaz will remain a black hole in the state finances.¹⁸ If such a situation continues, the re-politicization of bilateral gas relations, which has already begun with the Kharkiv accords, could increase substantially.

Thus on the domestic level, the interest of the Kharkiv accords and rapprochement with Russia should be understood as economic rather than ideological moves. Despite his history of close political relations with officials in Moscow, Yanukovych does not wish to align Ukraine with Russian policies completely.

¹⁵ IMF, *op. cit.* [13], p. 3; D. Fean, *op. cit.* [6], p. 418-419; EBRD Macro Economic Indicators, accessed March 2011,

<<http://www.ebrd.com/pages/research/economics/data/macro.shtml>>.

¹⁶ S. Pirani, J. Stern and K. Yafimava, *op. cit.* [12], p. 14.

¹⁷ Interview with gas expert, June 2010.

¹⁸ Interview with EBRD representative, June 2010.

Military Reform: A Heritage of Economic Constraint

The interaction of economic and security issues are of particular importance to the progress of Armed Forces reform. Yanukovich's abandonment of NATO integration raises questions about the future of the ongoing military reform program. While Ukraine's draft military doctrine foresees increased cuts to manpower, it appears that the overall reform objectives are to follow the lines laid out in 2005. In this area, economic concerns are primary: the consistent underfunding of military programs—even under the Orange coalition—has meant that these are running behind schedule and that expectations may have to be lowered. The economic crisis has had a catastrophic impact upon the financial position of the Armed Forces, and it will take significant funding increases to recover the time lost.

Armed Forces reform

Despite changes in the official policy on NATO, Ukraine continues to pursue reform efforts based upon the Western model of modern armed forces, with an accent on interoperability and international cooperation. Even if NATO membership is no longer an aim, Ukraine is trying to create Armed Forces in its image. The modernization of the Ukrainian military to Western model will continue under Yanukovich, as senior MoD officials confirm.¹⁹ This is not surprising as the Western, and more particularly US, military model represents the paradigm for the modern military—a point confirmed by Russia's military reform program, which also prioritizes interoperability, mobility and rapid deployment.²⁰

The State Program for Development of the Armed Forces 2006-2011 has established a number of objectives for the transformation of the armed forces. The military has been restructured into three divisions, aiming to increase interoperability: the Joint Rapid Reaction Forces (JRRF), Main Defense Force (MDF) and the Strategic Reserve.

¹⁹ Interview with senior Ministry of Defense official, June 2010.

²⁰ D. Sanders, "Ukraine's Military Reform: Building a Paradigm Army," *Journal of Slavic Military Studies*, Vol. 21, No. 4, 599-614, 2008; S. Blank, "No Need to Threaten Us, We Are Frightened of Ourselves," Russia's Blueprint for a Police State, The New Security Strategy," in S.J. Blank and R. Weitz, *The Russian Military Today and Tomorrow: Essays in Memory of Mary Fitzgerald*, Carlisle PA, US Army War College, 2010, p. 109.

The Joint Rapid Reaction Forces have been established and are responsible for international peacekeeping operations and crisis response. Despite its numerical size, numbering 29,000 or 30% of the total military by 2011 (as planned in 2006), the JRRF have a clear priority in funding and training terms, receiving a third more financing than the MDF despite representing less than half its numerical strength.²¹

The Main Defense Force operates at a lower rate of readiness; its primary responsibility is for territorial defense. Relative to its size, the MDF has been given a particularly low proportion of funding in recent years, and lower priority in many aspects of the training regime. Ukrainian analysts question this repartition of funds, arguing that such a strategy risks the creation of a two-tier system of military training.²²

Obstacles to reform

A number of obstacles frustrate the successful implementation of the reform program. Low salaries in the Armed Forces make it hard to attract the best candidates and it is not uncommon for military personnel to moonlight as security staff for private businesses in order to supplement their income.²³ Indeed, the Ministry of Defense has concluded that salaries are too low to make the military an attractive career. The minimum monthly allowance for a first year contract soldier in 2009 was 821 UAH (82 euros), less than half the national average and comparing unfavorably with the lowest paid agricultural sector workers (average of 1,240 UAH; 124 euros).²⁴ Even during the financial crisis, the MOD maintained that it was unable to compete with other employment sectors.²⁵

Significant time has been lost due to the political paralysis of the Orange period. Texts for laws were elaborated, but awaited adoption or debate in the Rada because of the perpetual crises in Ukrainian politics.²⁶ As dire issues of economic and political importance have monopolized the political agenda in recent years, not to mention almost constant electoral campaigning, the progress of military reform has become a secondary priority.

The current vision for the armed forces reform remains dependent upon reconciling the defense needs of the state with the budget given to the Ministry of Defense. Since independence, force reductions have seen the number of military personnel in Ukraine drop from 900,000 in 1991 to 165,000 military personnel (of a total 221,000 MoD staff) in 2006. Since 2007, the MoD staff levels have been capped at 200,000, of which the number of men under arms in 2010 was mandated to be 159,000.²⁷ In July

²¹ D. Sanders, *op. cit.* [20], p. 605.

²² Interview with Ukrainian analyst, June 2010.

²³ Interview with European Defense Team, 2009.

²⁴ Ministry of Defense, *White Book 2009*, Kyiv, 2010, p. 47. Exchange rate of UAH 9.99 to EUR 1 as at end of January 2009.

²⁵ Ministry of Defense, *op. cit.* [24], p. 49.

²⁶ Interview with European Defense Team, March 2009.

²⁷ Ministry of Defense, *op. cit.* [24], p. 78.

2010, it was announced that Ukraine would continue the process of reducing the number of soldiers in its armed forces by another 20% by 2015—to roughly 127,000.²⁸ During the process of drafting the new defense doctrine, plans were also made to increase the proportion of contract military staff from its current level of 52% to 90-100% by 2015, eliminating the need for conscript soldiers entirely. Under the 2006 plan, an entirely professional force of 143,000 was expected by 2011,²⁹ this is a clear demonstration of the failure to implement reforms effectively during the Orange era.

Leading Ukrainian defense analysts have criticized the 2010 announcement on the basis that the renunciation of NATO membership increased the responsibilities of the Armed Forces as they would no longer be expecting the article five guarantee of collective response to military aggression. They also estimated that the budgeted funds were only capable of maintaining an army of 110,000-140,000; yet, if the MoD intends to raise the standards to the level current in Central Europe, they estimated that only 50,000-60,000 military personnel could be kept.³⁰

Funding the reform

Even before the crisis hit in 2008, Western analysts were arguing that the ambitious reform and equipment programs would not be completed without improved funding.³¹ Funding for the MoD is split between the General Fund (from the central budget) and the Special Fund (allocated by the government from revenue generated by the Armed Forces from the sale of surplus equipment or real estate).

Following the economic crisis, the proportion of funds allocated from the Special Fund has increased from 10% of the total budget in 2008 to 33% in 2009. The government also established a Stabilization Fund in 2009, in order to prevent the decline of the armed forces during the economic crisis. The Special Fund often fails to deliver its budget allocation in full. As such, greater reliance upon Special Fund allocations makes the financial situation of the armed forces precarious. In 2008, the shortfall in Special Fund delivery led to a 3.8% budget deficit overall.

In 2009, the situation was even worse, with only 13.9% of the Special Fund allocation being delivered (only UAH 588.4 million of UAH 4.22 billion delivered in 2009): amounting to UAH 3.63 billion in promised funds not received. To exacerbate matters, the Stabilization Fund only delivered 35.8% of the amount promised (a further UAH 741.9 million deficit). In total in 2009, the military budget of UAH 12.8 billion was only

²⁸ Author's calculation based on figures from Ministry of Defense, *op. cit.* [24], p. 78.

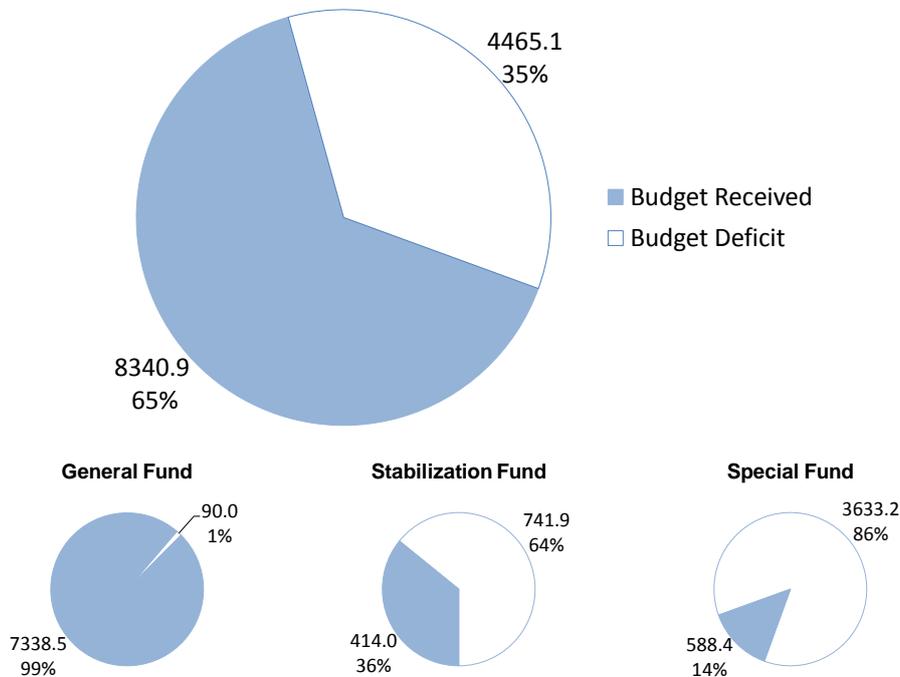
²⁹ NRCU, "Contract Army Will Prevail in Ukraine in 2015," 8 December 2010, <www.nrcu.gov.ua/index.php?id=148&listid=135198>.

³⁰ Razumkov Center, "Expert's Comment: 20% Troops Reduction is Forced and Contrary to Ukraine's Refusal of NATO Membership," 23 July 2010, <www.razumkov.org.ua/eng/expert.php?news_id=2329>.

³¹ D. Sanders, *op. cit.* [20], p. 606.

fulfilled by 65% (835 million euros out of 1.28 billion euros budgeted).³² The difficult economic conditions left Defense Ministry officials describing 2010 as a year of stabilization after the hardship of 2009.³³

Fig. 1. Defense Ministry Budget Implementation, 2009
Measured in UAH millions



Source: Defense Ministry of Ukraine, *White Book 2009*, Kyiv, 2010, p. 76

Defense budgets for 2010 and 2011 are more reassuring. In 2010, the MoD was allocated UAH 11.3 billion: UAH 8.67 billion from the General Fund and UAH 2.66 billion from the Special Fund. In September 2010, Defense Minister Yezhel announced that the budget for 2011 would stand at UAH 13.6 billion, an almost 20% increase on the figure for 2010. In addition, the allocation from the Special Fund is set at UAH 2.4 billion: still high but a more reassuring proportion of 17.6% given consistent failure to deliver.³⁴

Significant problems are caused by the fact that budgeting processes fail to take inflation into account.³⁵ In recent years, despite annual increases in budget figures, the budget has been cut in real terms. This can be seen in the dollar values of the defense budget in 2008-2009. The budget set at UAH 9.49bn in 2008 was worth US\$ 1.8bn; the 2009 figure of UAH 11.65bn was worth only US\$1.41bn.³⁶

³² Ministry of Defense, *White Book 2008*, Kyiv, 2009, p. 84; Ministry of Defense, *op. cit.* [24], p. 76.

³³ Interview with senior Ministry of Defense official, June 2010.

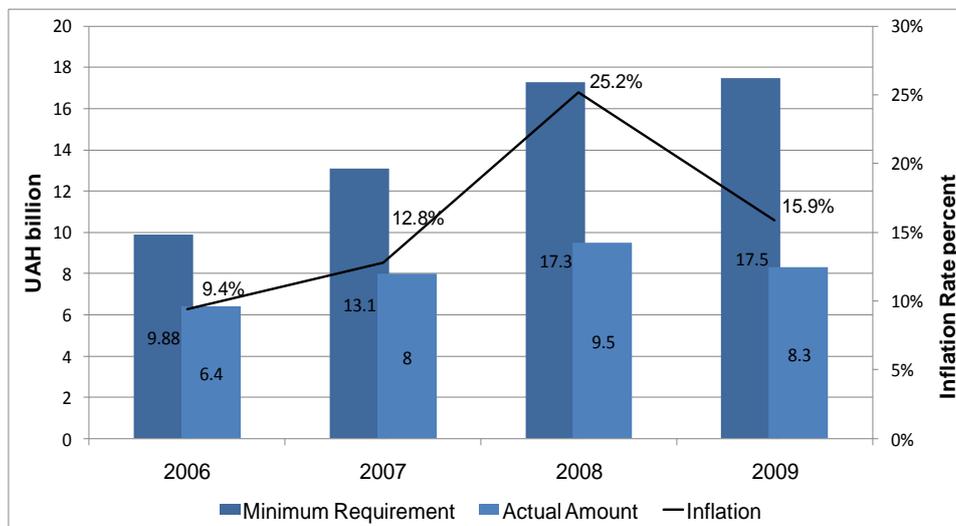
³⁴ "Defense Budget (Ukraine)," *Jane's Sentinel Country Risk Assessments - Russia and the CIS Countries*, 11 October 2010.

³⁵ Ministry of Defense, *op. cit.* [24], p. 19.

³⁶ IISS, *The Military Balance 2010*, London, Routledge, 2010, p. 195.

Further problems for the armed forces are caused by the fact that the official budget levels do not take into account the real cost of the responsibilities that fall to the Armed Forces; the level of funding often has no correlation to the requirements of State Programs intended to orientate defense reforms, for example. The MoD's assessment for the minimum annual requirement for reform is charted against the actual budget delivered in the chart below, putting the required funds for 2009 at UAH 17.5bn; MoD communications underline that the standard figure would be UAH 32.4bn as defined in the State Program for Development of the Armed Forces. Since 2006, there has yet to be a year in which even the minimum funds necessary have been received.³⁷

Fig. 2: Funding of the Armed Forces against Inflation 2006-2009



Source: Ministry of Defense, *White Book 2009*, Kyiv, 2010, p. 19.

Underfunding does not only affect the ability of the Armed forces to implement reform, it also leads to a drop in military preparedness. Before the crisis, flight hours for the Air Force were far below the NATO average: 70 hours for the JRRF and only 30 hours for the MDF; compared with a NATO average of 180h. In 2009, these figure plummeted: the JRRF managed just over 18h out of a planned 160h while the main defense forces completed fewer than 6h of a planned 20h.³⁸

The question of funding for the Armed Forces reform program corroborates the observation that for Ukrainian politicians, national defense issues are a secondary priority. In this respect, the failure to properly finance military programs calls into question the commitment of not only the government under Yanukovich, but also the governments under Yushchenko.

³⁷ Ministry of Defense, *op. cit.* [24], p. 19.

³⁸ D. Sanders, *op. cit.* [20], p. 611; Ministry of Defense, *op. cit.* [24], p. 82.

Domestic security as the priority

Low concern for the state of the armed forces could also be due to the threat assessments of the Ukrainian elite, which prioritize internal stability over territorial defense.³⁹ Indeed, in Ukraine the troop numbers for security services—including the Security Service of Ukraine, Interior Ministry Troops and Border Service—are 2.5 times the number of Armed Forces military personnel.⁴⁰ In Russia similar trends are visible, with domestic security spending exceeding the military budget—despite rhetoric of external threat.⁴¹

The instrumentalization of these bodies by the political elite is troubling, particularly as competition between the presidency and the Rada grew during the Orange period when different services were subordinate to the presidency and the government.⁴² Controversy over the security services has increased under Yanukovich. Yanukovich has also been criticized for using the Ministry of Interior troops (MVS) to dissuade opposition activities: the MVS have attended opposition rallies in full riot gear, seen as a means of dissuading the public from joining the protests.⁴³ The detention by the SBU of an official from a German political foundation in June 2010 was seen as a warning shot to civil society actors.⁴⁴ Foreign diplomats were later briefed to remain non-partisan in their activities.⁴⁵ Such developments resemble the actions of the Russian government to stave off potential “color revolutions”; such concerns may explain the addition of a line in the new Ukrainian defense doctrine on the role of outside powers in domestic politics.⁴⁶

³⁹ T. Kuzio, “The Non-Military Security Forces of Ukraine,” *Journal of Slavic Military Studies*, Vol. 13, No. 4, December 2000, p. 30.

⁴⁰ G. Mernikov, O. Kuplevetskaya, Finansirovanie silovikov v Ukraine : problemy i orientiry [Financing of force structures in Ukraine, problems and reference points], *Flot 2017*, 18 May 2010, <www.flot2017.com/show/analytics/23957>.

⁴¹ S. Blank, *op. cit.* [20], p. 90-91.

⁴² For example: SBU agents raided Naftogaz’s headquarters during Yushchenko’s dispute with Tymoshenko over the 2009 gas contract. In May 2007, when Yanukovich was Prime Minister, Vasyl Tsushko the Minister of the Interior tried to use the troops of the Ministry of the Interior (MVS) in a standoff with Yushchenko. The then-president re-subordinated the MVS to himself by decree, this lasted until May 2008 when he was obliged to return them to government control. G. Bennett, “The SBU—The Security Service of Ukraine,” Conflict Studies Research Centre, Central Asia & Eastern Europe Series 04/25, September 2004, p. 4-5, 17-19; L. Polyakov, “‘Paramilitary’ Structures in Ukraine,” in *Almanac on Security Sector Governance in Ukraine 2010*, Geneva Centre for the Democratic Control of Armed Forces, Geneva, 2010, p. 134, 148; RFE/RL, “Ukrainian Security Service Raids Gas Firm HQ,” 4 March 2009, <www.rferl.org/content/Ukrainian_Security_Service_Raids_Gas_Firm_HQ/1503960.html>.

⁴³ T. Kuzio, “The ‘Putinization’ of Ukraine’s Security Forces,” *Eurasia Daily Monitor*, Vol. 7, No. 120, Jamestown Foundation, 22 June 2010.

⁴⁴ Interviews with Ukrainian think tank experts, June 2010.

⁴⁵ Interviews with Ukrainian analysts, Western diplomat, June 2010; Russia Today, “Ukraine Approves New Military Doctrine,” 14 April 2011, <<http://rt.com/politics/ukraine-new-military-doctrine>>.

⁴⁶ T. Ambrosio, *Authoritarian Backlash, Russian Resistance to Democratization in the Former Soviet Union*, Farnham, Ashgate, 2009, p. 45-53.

Thus it is not just the Armed Forces that need to be taken into consideration when thinking about security reform in Ukraine. Armed Forces reform is relatively un-contentious, being of low importance to the domestic political scene. Security sector reform was discussed in 2006, but since almost every actor attempted to use the services under their control to reinforce their political position the reform lacked conviction.⁴⁷ Without the process of NATO integration and with decision-making power having been re-centered within the Presidential Administration in 2010, interest in reforming the security sector may dissipate.

Yanukovych may not see reform of the security sector as a priority

Having returned control of all security structures to the presidency, Yanukovych may no longer see their reform as a priority: particularly as they do not threaten regime stability in their current form. This is particularly true as their current configuration allows their use to pressure opposition.

Analysis of the financing and shape of military reform clearly shows that despite a clear desire not to antagonize Russia, Ukraine continues to have an attachment to a Western model for armed forces reform. It also hints that domestic security concerns have been privileged by the political elite in Kyiv for some time, despite the rhetorical attachment to armed forces reform during the Orange period.

⁴⁷ L. Polyakov, *op. cit.* [42], p. 149, 158.

Non-Bloc Status: Back to the Middle Ground

Among Yanukovich's first acts after consolidating his position by forming the "Stability and Reform" coalition was the "On the Principles of Domestic and Foreign Policy" passed in July 2010. Under this law he enacted the foreign policy priorities laid out in the coalition agreement. Namely: fixing of Ukraine's non-bloc status at the legislative level and reparation of relations with Russia on the basis of strategic partnership, friendship, and good neighborliness.⁴⁸ As previously noted, the new government has no objections to the military reforms elaborated with the help of NATO. Indeed, Ukraine under Yanukovich has maintained a close relationship with the Atlantic alliance, continuing technical cooperation at numerous levels. While renouncing membership of NATO may improve Ukraine's relationship with Russia, it is not abandoning its ties to the alliance.

Yanukovich has declared that relations with Russia should be repaired to return balance to the country's foreign policy. Indeed, his defense of a more equal foreign policy can be seen as a return to the "multi-vectoral" foreign policy of Kuchma. As noted above, balance in relations with Moscow is important, due to the cultural identities of the different regions. Relations need to be separate and sovereign to satisfy the attitude of the Western regions, but friendly in order to satisfy the concerns of the Eastern regions.⁴⁹

This decision to legislate Ukraine's "non-bloc" status has been understood to represent a direct concession to Russia, given Moscow's—particularly Vladimir Putin's—vehement objections to Ukraine's inclusion in NATO.⁵⁰ It was also specifically mentioned in an August 2009 address from President Dmitry Medvedev as one of a number of Russian grievances against Viktor Yushchenko.⁵¹

The domestic and budgetary factors which led to these moves already having been elucidated, it appears that the motivations of security policy decision-making under Yanukovich should be understood as separate from the strategic effects that they have had.

⁴⁸ BBC Monitoring, "Ukrainian Paper Publishes Text of New Parliamentary Coalition Agreement," 18 March 2010; Ukrainian National Information Agency, *op. cit.* [2].

⁴⁹ R. Legvold and C. Wallander (eds.), *Swords and Sustenance: the Economics of Security in Belarus and Ukraine*, Cambridge MA & London, MIT Press, 2004, p. 10.

⁵⁰ P. Finn, "Putin Threatens Ukraine on NATO, Russian Raises Issue of U.S. Missile Shield," *Washington Post*, 13 February 2008, <www.washingtonpost.com/wp-dyn/content/article/2008/02/12/AR2008021201658.html>.

⁵¹ D. Medvedev, *op. cit.* [1].

Motives for the policy change

While Yushchenko considered Russia to be the primary threat to Ukraine, the new administration “for political reasons” cannot make statements which imply such a belief. As a result foreign partners have been briefed that Romania represents the largest military threat.⁵² Yet, the deal need not be seen as an ideological swing toward Russia by Yanukovych. Given the dire state of the economy and Kyiv’s weak bargaining position, a deal on the stationing of the BSF in Crimea was likely regardless of whether Yanukovych or Tymoshenko won the presidency in 2010. Ukrainian analysts and Western diplomats in Kyiv certainly expected some concession to be made on this issue.⁵³ What came as a surprise was that the gas issue and the question of the fleet be linked so directly.

There is ample proof that Yanukovych does not want to make Ukraine completely subordinate to Russia in strategic affairs. During the 2008 Georgia-Russia war, he may have voiced support for Russia, yet Yanukovych has not followed Russia in recognizing Abkhazia and South Ossetia as independent: his support of Russian actions in 2008 was politically expedient rather than ideological.⁵⁴ Yanukovych has renounced NATO membership (discussed below), but the law also prevents Ukraine joining the Russia-backed Collective Security Treaty Organization. As such the move conforms to the balancing policy which Kyiv declares to be its objective.

Government officials argue that since the Black Sea Fleet (BSF) has been present in Ukraine and regulated since 1997, the extension of the lease to 2042 does not change anything. According to Ministry of Defense (MoD) sources it was not an easy decision, but it results from the desire to increase the independence of the Ukrainian state, and above all its economic independence.⁵⁵ Indeed, even Ukrainian analysts who opposed extending the lease highlight Yanukovych’s pragmatism on this matter. From this point of view, the administration merely exchanged “scrap metal for cash.”⁵⁶ However, they may have been misguided: the signing of the agreement has prompted the Russian navy to elaborate an ambitious refit and upgrade program for the fleet.⁵⁷

It is important to highlight the politicization of the NATO issue in this context. Despite the rhetorical attachment to integration, Ukrainian politicians have been unable to implement the reforms necessary to bring membership closer to an objective reality.⁵⁸ Regardless of the fact that the possibility of membership was not even an immediate possibility, Ukrainian

⁵² Interview with Western diplomats, June 2010.

⁵³ Interviews with Ukrainian think tank, June 2010; Western diplomats, October 2009.

⁵⁴ T. Kuzio, “Strident, Ambiguous and Duplicitous: Ukraine and the 2008 Russia-Georgia War,” *Demokratyzatsiya*, Vol. 17, No. 4, Fall 2009.

⁵⁵ Interview with senior Defense Ministry official, June 2010.

⁵⁶ Interview with Ukrainian think tank, June 2010.

⁵⁷ M. Barabanov, “Big Renovation Program for Russia’s Black Sea Fleet,” *Moscow Defense Brief*, No. 3 (21), 2010.

⁵⁸ J. Simon, “Ukraine Needs to Decide its Strategic Alignment,” *Southeast European and Black Sea Studies*, Vol. 9, No. 3, 2009; interview with Western military experts, June 2009.

analysts have criticized the fact that NATO membership aspirations were abandoned “for free.” The contentious matter here is not that Yanukovich halted the NATO membership process; it is that he did so without extracting significant concessions from Moscow.⁵⁹ Given Russia’s vehement declarations against the move, Yanukovich could have expected to be rewarded handsomely for the move to abandon NATO membership. Thus even within the Ukrainian analytical community, the sacrifice of traditional security interests for economic ones is not an aberration, the complaint is that it has not been carried out well enough by Yanukovich.

Debate over Ukraine’s NATO membership also had strong domestic political underpinnings. Kuchma varied in his support for membership but ultimately balked at democratization which could challenge his power.⁶⁰ Public opposition to NATO membership is engrained: in multiple surveys since September 2004 the proportion of those surveyed that reject the move never dipped below 50% and remained around 69% for the two most recent polls (both 2009).⁶¹

Yanukovich has moved away from NATO membership, but stayed close to the alliance: non-bloc status does not prevent his administration cooperating with the alliance. As a senior Defense Ministry official explained, the priority in its relations with NATO now is to pursue pragmatic cooperation in accordance with Ukraine’s interests.⁶² Despite legislating for the non-bloc status of Ukraine, in November 2010 Yanukovich issued a decree establishing a Commission on Partnership with NATO subordinate to the Presidential Administration. This body appears to be a substitute for the bureau under the Cabinet of Ministers dissolved earlier in 2010.⁶³

Yanukovich has moved away from NATO membership, but stayed close to the alliance

Ukrainian Armed Forces personnel make a small contribution to NATO actions in Afghanistan (10 soldiers), Iraq (9) and a larger joint battalion (180) with Polish involvement in KFOR, NATO’s mission in Kosovo.⁶⁴ The reduced ambitions for Ukraine’s relationship with NATO do not call these engagements into question: they allow Ukraine to continue participating in high level international operations, and provide valuable combat experience to the forces undergoing reform.⁶⁵

⁵⁹ Interview with Ukrainian analysts, June 2010.

⁶⁰ M. Peterson Ulrich, *Ukraine’s Military Between East and West*, Carlisle PA, US Army War College, May 2007, p. 24; T. Kuzio, “Neither East nor West Ukraine’s Security Policy under Kuchma,” *Problems of Post-Communism*, Vol. 52, No. 5, September/October 2005.

⁶¹ Razumkov Center, “Ukraine Poll: How Would You Vote if the Referendum on Ukraine’s NATO Accession Was Held the following Sunday? (recurrent, 2002-2009),” accessed February 2011, <www.razumkov.org.ua/eng/poll.php?poll_id=46>.

⁶² Interview with senior Defense Ministry official, June 2010.

⁶³ “Decree by the President of Ukraine No. 1039/2010, On Further Constructive Cooperation of Ukraine with the North Atlantic Treaty Organization,” 18 November 2010, <www.mfa.gov.ua/mfa/en/publication/content/48821.htm>; D. Fean, *op. cit.* [6], p. 420.

⁶⁴ IISS, *op. cit.* [36], p. 197.

⁶⁵ Interview with Ukrainian military expert, June 2010.

Strategic effects of Yanukovich's policies

Strategically the Kharkiv accords are significant. Regardless of their rationale, they reinforce the Russian presence in Ukraine, reinforce the primacy of Russia's role as energy supplier and give the Kremlin significant leverage. Additionally, since they are an advance upon the rent paid for the base after 2017 and subject to annual approval by the parliament, Russia has significant opportunities to withdraw the subsidy should relations with Ukraine degrade again.

The maintenance of a Russian presence in Crimea is significant due to the importance that the Russian elite place upon its influence there. With a largely ethnic Russian population and short history of attachment to Ukraine,⁶⁶ Crimea remains a strong element of Russia's attachment to Ukraine. The significance of Crimea as a tool to pressure Kyiv has not been lost on Russian scholars who see the maintenance of this presence as a geopolitical boon.⁶⁷ Indeed, the Russian attitude to the deal appears to dovetail with the Ukrainian point of view: while Kyiv is subordinating geopolitics to economic expediency, Moscow is subordinating business rationale to *Realpolitik*.

Ukrainian experts note that there is nothing to be lost and everything to be gained from improving the relationship with Russia, but the manner in which it is being done is inappropriate: they believe that the government does not understand the ramifications of abandoning all alternative alliances.⁶⁸

Outlook

More concessions to Russia on security or economic issues are to be expected: Yanukovich is keen to secure further reductions in the gas price and the sustainability of the 2009 contract has been called into question.⁶⁹ The reduction of 30% does not improve the profitability of Ukrainian industry significantly, taking into account the fact that Ukraine already enjoyed a 20% reduction in 2009. In addition, Kyiv argues that the price formulae are disadvantageous to Ukraine. Oil prices—upon which the base price is calculated—were rising steadily even before the recent troubles in the Middle East and North Africa. High oil prices only make further deals more likely.

Nevertheless, officials in Kyiv have skillfully circumvented Russian proposals which they judge disadvantageous. Offers to merge Naftogaz with Russia's Gazprom and for Ukraine to join the Russia-Belarus-Kazakhstan Customs Union have been skillfully put aside by Ukrainian

⁶⁶ Crimea only became part of the Ukrainian Soviet Socialist Republic in 1954.

⁶⁷ M. Barabanov, *op. cit.* [5], p. 8-10.

⁶⁸ Interview with Ukrainian military analyst, June 2010.

⁶⁹ S. Pirani, J. Stern and K. Yafimava, *op. cit.* [4].

officials.⁷⁰ Furthermore, if Tymoshenko is prosecuted for abuse of office—prosecutors accuse her of exceeding her mandate by signing the 2009 contract—the Ukrainian government could call the entire contract into question; at the very least Ukrainian demands to renegotiate the pricing formulae would have to be taken more seriously by Russia.

Certain representatives of the analytical community continue to support NATO membership as a means to promote Ukraine's democratization and integration with the West. According to one such analyst, the return of a strong Russian vector in Ukraine's international relations means that NATO has lost Ukraine as an equal partner since Russia will only allow Ukraine a relationship that is subordinate to its own relationship with the Alliance.⁷¹ Even if official policy is to continue cooperation, Ukrainian experts are doubtful: they believe that the rapprochement with Russia will lead to a point where Moscow is no longer comfortable with Ukraine's relationship with NATO, resurrecting tensions over the Ukraine-NATO relationship.⁷²

The promise of future membership made at NATO's 2008 Bucharest summit stands: NATO's door remains open, as US Secretary of State Hillary Clinton repeated in July 2010.⁷³ Yet, the Kharkiv deals—particularly their being a loan against future rent—open the opportunity for Russian meddling should NATO membership become a real possibility. That is without mentioning the fact that the presence of a Russian military base in Ukraine will prevent the latter's accession to the alliance.

⁷⁰ The former would leave Ukraine with a minority stake in the merged entity, while the latter would prevent Ukraine from signing the Deep and Comprehensive Free Trade Agreement with the EU under negotiation.

⁷¹ Interview with Ukrainian analyst, June 2010.

⁷² Interview with Ukrainian military expert, June 2010.

⁷³ State Department, "Town Hall at Kyiv Polytechnic Institute," 2 July 2010, <www.state.gov/secretary/rm/2010/07/143941.htm>.

Conclusion

The decisions made by Viktor Yanukovych since he became President of Ukraine in February 2010 have had a profound impact upon the regional distribution of influence. His signing of the Kharkiv agreements exchanged continuing Russian influence over Ukraine's strategic posture for cheaper gas prices in support of the interests of his oligarch backers. The legislation of Ukraine's non-bloc status reoriented Ukraine in its cooperation with NATO: for the foreseeable future cooperation will be technical, with no membership ambitions.

While the changes did play to Russian interests, they are not a sign of Yanukovych's subjugation to Moscow in defense matters. Rather, they represent his prioritization of economic matters, particularly the interests of his entourage. It should also be remembered that the price reduction allowed the new government to rekindle Ukraine's cooperation with the IMF: Russian money was not the only incentive.

While these accords were judged necessary in order to improve the economic stability of the country and its relations with an important neighbor, they have opened the door to increased Russian influence in the future. The gas agreement is structured in such way as to invite further problems, and the Kyiv government has made it clear that it would like to see even greater reductions—although not at all costs. The continued basing will allow Russia to continue to exert significant pressure on Kyiv via its manipulation of Russian nationalist sentiment on the Crimean peninsula.

Defense and reform have appeared to be secondary issues for the Ukrainian elite, the format of the Orange government's reform program is approved by the new authorities as confirmed by the continuation of cooperation with NATO. The failure of the Yushchenko era to properly finance these reform efforts indicates that even for this strident supporter of NATO integration, the Armed Forces were not a priority.

Reform is likely to continue in the Armed Forces as a clear program exists and the process is not contentious; in the domestic security sector, this may not be the case. The removal of NATO membership as an objective increases the space for Yanukovych to reform this sector as he sees fit or indeed to leave it much the same: this is particularly troubling in light of the previous experience of the security services being used for political ends. Coordinated domestic and international pressure for Yanukovych to address this issue should lead to results.