Analyses OSW

CENTRE FOR EASTERN STUDIES 18.12.2013 www.osw.waw.pl

The Moscow deals: Russia offers Yanukovych conditional support

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A number of documents enhancing the co-operation between Russia and Ukraine, above all concerning the economy, were signed during the meeting of Presidents Vladimir Putin and Viktor Yanukovych on 17 December in Moscow. The most important arrangements include the decision to offer Ukraine temporarily reduced prices of gas supplied from Russia and the declaration that Russia will buy Ukrainian Eurobonds. These preferential conditions will allow the Ukrainian government to stabilise the country's extremely difficult economic situation within a short timeframe. Furthermore, they will provide Kyiv with good grounds to withdraw from becoming associated with the EU and to prioritise its co-operation with Russia. This may bolster the position of President Yanukovych in the period preceding the Ukrainian presidential election in 2015. It appears that Russia has deemed that re-election of the incumbent Ukrainian president will offer it a guarantee that its interests will be respected to the greatest extent, and has thus decided to back him. However, this support is conditional and involves preventing Ukraine from establishing closer relations with the EU and Ukraine will most likely be expected to gradually introduce economic concessions for Russia. Ukraine's accession to the Customs Union is a strategic goal for Russia, and Moscow hopes this will happen after the Ukrainian presidential election in spring 2015.

The results of the meeting

An annexe to the contract between Russia's Gazprom and Ukraine's Naftogaz covering gas supplies to 2019 was signed during the meeting in Moscow. The gas price offered to Ukraine was temporarily reduced from the present level of approximately US$400 to US$268.5 per 1,000 m3. According to a document published by Russia's Interfax-Ukraine News Agency, the parties (*de facto* Gazprom) will agree on the level of the price reduction quarterly, starting from 1 January 2014. Putin also announced that Russia would invest US$15 billion from the Russian National Welfare Fund in Ukrainian Eurobonds. The Russian Minister of Finance, Anton Siluanov, added after the meeting that by the end of 2013 Russia would acquire Ukrainian bonds to a value of US$3 billion for two years at a 5% interest rate. Possible further acquisitions will be made "if needed". However, no formal document regarding the purchase of bonds was signed. What were signed during the meeting were: an action plan envisaging the removal of barriers to mutual trade and eleven co-operation agreements in the areas of the aviation industry (the implementation of the An-124 cargo airplane project), the shipbuilding and rocket-and-space industries, a nuclear early warning system, the liquidation of the consequences of catastrophes and natural disasters, co-

operation between customs and border control services, and the construction of a bridge over the Strait of Kerch. Putin and Yanukovych emphasised that they had not discussed the prospects of Ukraine's integration with the Customs Union.

Russia's goals

The announced decisions to offer support to Ukraine are aimed at portraying Russia as a partner who, unlike the EU, is capable of rendering tangible assistance. It appears that the Kremlin's decisions to grant the preferential terms to Kyiv have been affected by the tense domestic situation in Ukraine – it had been expected earlier that the gas prices would be reduced for Ukraine on condition that it granted consent for a gradual integration with the Customs Union. Although the Russian government still views Ukraine's membership of the Customs Union as a strategic goal in its policy towards Kyiv, it has not decided to use the Moscow meeting to make any arrangements to this effect. Russia is aware of the fact that this would have provided new stimuli for the escalation of protests in Ukraine. It still needs to be emphasised that not all the details of the announced deals are known, nor are the contents of possible informal arrangements. The real terms and cost of Russia's support are thus still unclear. The information which has been revealed so far signifies that the agreements include mechanisms which make Russia's assistance dependent on the stance taken by the Ukrainian government. Thus Moscow has secured itself against possible attempts Kyiv may make to reduce its dependence on Moscow or to resume co-operation with Brussels. Furthermore, the Ukrainian economy will be ever more bound to Russia as a consequence of the implementation of these deals. It appears that the Kremlin has decided to continue supporting Viktor Yanukovych until the Ukrainian parliamentary election in 2015. From Moscow's perspective, Yanukovych, who has been deprived of the possibilities of real co-operation with the West and who will owe his victory to Russian support, will be the president best able to guarantee that the Russian goals concerning Ukraine are achieved. Forcing Yanukovych to grant consent for Ukraine to become integrated with the Customs Union will be an essential element of the price he will have to pay for Russia's support. Moscow is clearly hoping that this could happen after the Ukrainian presidential election in spring 2015.

Ukraine's goals

From the documents signed in Moscow, the Ukrainian government considers the most important ones to be the deals for a reduction in the gas price for Ukraine and the purchase of Ukrainian bonds as a form of Russian support for Ukraine's public finances. These will *de facto* save Ukraine from bankruptcy and make it possible for next year's budget to be adopted. The government in Kyiv had been postponing the announcement of the draft budget until a new price for Russian gas was set. Given the disastrous financial situation Ukraine has found itself in this December, the Russian promise to buy Ukrainian bonds is of key significance for Kyiv. The bonds, with interest rates half that at which Ukraine is attempting to take out loans on the international financial markets, will allow Ukraine to close its budget gap this year and next year, and also to handle its foreign debt.

If the new gas price is maintained all year long, Ukraine will save at least US$2.5 billion, provided that the state-owned company Naftogaz maintains imports at the same level as in 2013, i.e. 18 billion m3 of gas. It could save even more if more gas was imported from Russia, but it would have to discontinue gas supplies from the EU. At the same time, this would mean that Gazprom could maintain its income from exports to Ukraine at the same or an even higher level. The need for Naftogaz to obtain price approval from Gazprom on a quarterly basis offers Moscow more opportunities to apply pressure on Kyiv.

The aggregate maximum benefit Ukraine could get as part of the assistance offered by Russia could exceed US$17 billion. By Ukrainian standards, this is a huge sum. If the government had such money at its disposal, President Yanukovych could implement his welfare policy in 2014 without the need to carry out unpopular reforms which the West required from Kyiv as a condition for offering possible loans as a form of assistance. This would significantly strengthen Yanukovych's position in the context of his struggle for re-election. He will attempt to utilise the results achieved in Moscow to his advantage in the electoral campaign, especially while addressing his electorate in eastern Ukraine who traditionally hold pro-Russian views. It appears that the price Ukraine will have to pay for such great support from Russia could be not only Kyiv's earlier decision to in fact withdraw from entering into the Association Agreement with the EU, but also concessions made to Russia on the Ukrainian energy market, and most likely other concessions which have not as yet been made public.