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A lifeline for Ukraine from the IMF

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On 8 December the International Monetary Fund made changes to its longstanding policy, allowing the implementation of bailout programs for countries that are behind with their debt repayments of other countries, which had previously been forbidden. This decision will allow the IMF to continue its programme of support for Ukraine, which has refused to repay the US$3 billion debt to Russia (the deadline for which expires on 20 December) it incurred in December 2013. Both parties are in dispute concerning the nature of the debt, which Russia regards as an official loan and Ukraine as a commercial loan. Although it is *de facto* a sovereign debt, Kyiv maintains that formally it is a private loan, and that the creditor is the Russian National Wealth Fund. On 16 December, the IMF ruled on this debt as an official.

Commentary

- The IMF's decision is of great importance for Ukraine, which is in a very difficult financial situation; during the first nine months of this year, its external public debt rose by 20% to US$46.5 billion, while its foreign exchange reserves amounted to US$13 billion at the end of October. With this decision, the IMF will be able to continue its four-year support programme, worth US$17.5 billion dollars, which is Ukraine's main source of external funding and a framework for its reform agenda. Repaying the Russian loan on time would cause Ukraine's finances to deteriorate, and would be met by strong domestic opposition due to the continuing conflict with Russia.
- Kyiv is seeking a restructuring of its debt to Russia at the very least, and ideally hopes that the repayment will be blocked. Ukraine has questioned the legitimacy of repaying the debt, which former President Viktor Yanukovich incurred for political reasons (Russia granted the loan in exchange for Ukraine's refusal to sign the Association Agreement with the EU), as well as in the light of the ongoing war in the east of the country and the occupation of Crimea. Kyiv is treating the loan as a private debt which can be restructured. At the end of August, Ukraine reached an agreement with private creditors on the haircut of 20% of the US$18 billion of debt and extending its maturity. Similar conditions were presented to Russia, but it rejected them.
- The IMF's decision is a defeat for Russia's policy, which sought to block the financial support programme for Ukraine. Moscow initially refused to hold talks with Kyiv on debt restructuring; it then demanded that Ukraine repay the debt from the funds of its foreign financial aid; and finally, Moscow unveiled its own proposal to restructure the debt (extending the deadline by a year and redistributing it into three tranches under Western

guarantees) which would have been unfavourable for Ukraine and the West. Russia sees the debt issue as an instrument of political pressure in its conflict with Kyiv.

- While the IMF's decision concerns the entirety of its policy, the key motive for the change was the financial conflict between Ukraine and Russia, and Western countries played an important role in the decision. Russia has criticised the IMF's move and announced it will take legal action. According to the loan agreement, any disputes are to be resolved before either the British courts or the London Court of International Arbitration, which will probably take at least one or two years. The Ukrainian-Russian financial conflict has thus been transferred away from the IMF and its resolution postponed. This should give Kyiv the time it needs to stabilise the economic situation and implement the necessary reforms.