Ukraine's Neoliberal War Mobilization

Friday 10 February 2023, by COOPER Luke (Date first published: 30 January 2023).

Low taxes, privatization, and pared-back labor protections could undermine Ukraine's fight against Russian aggression.

In the early 1980s, following the death of strongman founder Josip Broz Tito, Yugoslavia's economy broke down. The United States had abruptly hiked interest rates, forcing up the cost of borrowing and making it nearly impossible for the Eastern European federation to pay back foreign debt. And, in the wake of Poland's 1981 financial collapse, foreign investors lost confidence in Yugoslavia's economy, demanding repayment on their loans.

The International Monetary Fund (IMF) was active in Yugoslavia by June 1980, almost immediately following Tito's death, and became steadily more involved as the 1982-1983 global debt crisis took hold. The Fund stepped in with a $6.5 billion emergency lending package in 1983 demanding a policy framework based on high interest rates, an austerity budget, wage suppression, and the abolition of price controls.

These were all measures consistent with the neoliberal turn pioneered in the West by President Ronald Reagan and British Prime Minister Margaret Thatcher, a program that sought to radically reinforce the power of capital. IMF emergency lending programs were critical in globalizing this agenda.

> "Given neoliberalism's bloody history in Eastern Europe, it may come as a surprise that free-market orthodoxies remain popular."

But neoliberal austerity wasn't simply imposed on elites in the Global South. The IMF found enthusiastic supporters for its agenda in recipient countries. One such figure was Yugoslav Deputy Prime Minister Borislav Srebic. "We made a mistake when we socialized the factor of risk," he said in 1982, commenting on the refusal of the old planning system to shut down unprofitable factories. "We want to see that those who disrespect economic laws are punished."

Rate hikes and the global energy price shock brought a foreign-born crisis to the doorsteps of ordinary Yugoslavians, triggering inflation, wiping out the standard of living, and inflaming tensions between conservative rural areas and the urban liberal classes. It was a form of crisis that would become increasingly common: Over the last 40 years, states from Somalia to Sri Lanka have experienced remarkably similar political and economic convulsions.

In many of these crises, the IMF would appear on the scene, offering emergency lending—but only in exchange for a brutal program of economic restructuring and liberalization. International creditors' emphasis on debt repayment and inflation-fighting often came at a huge cost to the well-being of ordinary people—and in some cases, hastened the collapse of the state itself.

The IMF's history as a policeman for global creditors in the '80s and '90s is well known. Today, the Fund's public face is much gentler. Managing Director Kristalina Georgieva speaks passionately about the urgency of greater investment and concessional lending to the developing world. Yet even as neoliberalism has fallen out of fashion in the IMF's rhetoric, old tendencies persist. While the Fund temporarily relaxed its most stringent policies in response to the COVID-19 pandemic, opening liquidity windows and appearing to favor a more countercyclical approach, it is now calling for fiscal consolidation, insisting on austerity budgets in countries that remain saddled with debt.

Given neoliberalism's bloody history in Eastern Europe, it may come as a surprise that free-market orthodoxies remain popular with an influential segment of the region's elites. Following Russia's invasion early last year, Ukrainians responded with heroism and determination, beating back President Vladimir Putin and his imperialist designs. But while Ukraine's military prowess has confounded the initial pessimism of observers, we may now be at risk of becoming too sanguine about Ukraine's continued success.

In my recent research report, I show that while Ukraine's success on the battlefield has been more successful than anticipated, buoyed by an upswell of civic spirit and Western military aid, the mobilization could still be imperiled by Ukraine's insistence on a radical free-market economic agenda.

Economic Liberalization and Intractable Violence

Yugoslavia's tragic collapse would become a paradigmatic example of the type of wars that would later blight the 21st century. The pursuit of economic liberalization in countries with political authoritarianism and ethnic sectarianism has tended to set off conflicts that entrench cycles of violence.

Syria's Baathist regime, which has ruled the country since 1963, undertook a decade of economic liberalization in the 2000s, leaving the country rife with unemployment and poverty on the eve of its failed revolution and subsequent civil war. The administration of George W. Bush pursued neoliberal restructuring of occupied Iraq, dismantling state capacity and sinking the country into corruption and sectarianism. Under the cover of "de-Baathification," thousands of civil servants and public-sector workers lost their jobs, the state became dysfunctional, and sectarian tensions were compounded.

In Sudan, the Democratic Republic of the Congo, and South Sudan, as well as Iraq and Syria, contests over rents from resources have driven violence and intercommunal tensions. Global financial pressures often play a hidden role in these conflicts. As capital can move effortlessly across borders, it has become exceptionally easy to hide the proceeds of corruption and fund armed groups. At the height of ISIS, it was thought to be selling oil and laundering proceeds of as much as $2 million a day.

The failure of the policies favored by the IMF and World Bank to achieve development goals has often created a vicious circle in conflict-affected regions. Falling income and production, high unemployment, and the availability of weapons are an incendiary mix. In the DRC's "checkpoint economy," armed groups set up roadblocks to levy informal taxes. Even multinational corporations like the beer-maker Heineken have become integrated into these informal networks as their trucks pay up at checkpoints. As this political economy of rebel finance takes shape, it can become self-perpetuating, with states losing legitimacy and rogue actors developing a greater stake in continuing violence.

Will Ukraine Become a "Forever War"?

These cases of intractable conflict provide a warning to Ukraine. The country's success on the battlefield to date reflects the deep support for the war effort and a popular willingness to endure terrible hardship to protect Ukrainian democracy and sovereignty. But this tremendous civic spirit cannot permanently offset Ukraine's severe economic crisis, which is being worsened by government policy.

Ukraine is currently in the throes of a war-induced economic recession, with as many as a third of job seekers unable to find work. Around a half of firms have reported cutting wages, in some cases by as much as 50 percent. Inflation sits at around 20 to 25 percent. In 2022, the state ran a deficit of $27.5 billion. This is not quite as bad as some initial projections anticipated, reflecting the country's progress in the war, which has allowed civilians to restart some economic activity away from the front lines. But Ukraine still faces a huge funding challenge for 2023.

When loans and aid haven't sufficed, the country has resorted to printing money—an emergency measure to continue to pay obligations like pensions but one that risks inflation. Successful war economies have historically held back from financing the budget deficit by issuing more money, because they recognized that inflation was a fundamental risk in a situation of scarcity due to the huge resource demands entailed by fighting the war.

Recognizing that markets cannot function in situations of all-out war, states fighting conventional wars have traditionally intervened extensively to make up for the fall in economic demand. During World War II, the Allies treated the economy as one big company, directing capital and labor to high-priority sectors.

The U.K. and the U.S. dramatically improved state capacity by raising additional tax revenue and steering it to military and humanitarian needs. They used price controls to tackle the dangers of inflation and war profiteering. And they struck negotiated agreements with organized labor to ensure that the costs of the war were met by those most able to pay.

You Can't Fight Wars With Neoliberal Economics

Ukraine has not developed a conventional war economy, and is instead combining some aspects of economic centralization with deregulation and privatization. Supporters of the Ukrainian government approach say this will facilitate economic growth. But the framework fails to take into account how "normal" market mechanisms fail under economic circumstances that are so volatile and inhospitable to private-sector investment.

Last summer, Ukraine's government introduced changes to the country's labor code that have removed 70 percent of the workforce from the protection of national labor law, including taking away their rights to engage in collective bargaining. British-style "zero hours" contracts, where workers have no idea how much work they will be given from one week to the next, were also legalized as part of this drive for flexible labor markets.

The government also announced a streamlined process for privatization, which has limited the conditions that the state can place on the buyers of public assets. Some 420 state-owned enterprises have so far been identified for sale. The first of the privatization auctions took place last September with some property of the state brewery company, UKRSPYRT, sold off. "The state should not manage businesses—a private owner will do it much more efficiently," said Yuliia Svyrydenko, Ukraine's minister of economy, in a press release entitled "Privatization Has Been Restored."

An all-out war is a bad time to maximize the value of these assets. They are likely to be sold off on the cheap, potentially compounding corruption problems and risking a rerun of the mistakes seen in the 1990s post-Soviet economic transition. The government has also stepped back from price controls, despite high inflation, claiming the use of them at the start of the war had failed.

Unshakeable belief in the self-regulating character of markets is a problem even in peacetime, but during war it poses calamitous risks.

The trade unions have not been brought into decision-making, and have bitterly opposed the government's labor reforms, while pointing out that under conditions of martial law, they are unable to organize protests against these measures.

Huge increases in military expenditures in Ukraine's 2023 budget have mostly been financed through steep cuts to other areas. While heavy spending on the war is understandable, Ukraine has refused to increase its domestic tax base. The self-employed pay a tax rate of just 5 percent and an additional war levy of 3 percent. Many salaried professionals are employed on these contracts to benefit from this ultra-low taxation.

Ukraine's tax system is in general highly regressive by international standards. Personal income tax is 18 percent, and there is no distinction in rate between high and low earners. Introducing a wealth tax or raising the corporate tax, which currently stands at 18 percent, could also support the war effort. Yet the government seems to be moving in the opposite direction. They are preparing a tax reform that would see corporation tax, income tax, and VAT (currently 20 percent) all cut to just 10 percent.

Where the IMF and World Bank might once have cheered on such a policy framework, they are today much more critical. The IMF warned prior to the full-scale Russian invasion that Ukraine's tax code is "relatively weak on progressivity." The World Bank has argued that "flat rates impose a disproportionate burden on the least well off." In light of this opposition, the Ukrainian government has launched a public campaign to persuade global lenders that its tax cuts are advisable.

The neoliberal home front is not the whole story. Ukraine has temporarily seized assets to facilitate the war effort, and a labor market public-works scheme is providing jobs to support the war effort and begin reconstruction. But as of January 2023, only around 5,000 workers have joined this "Ukraine Recovery Army."

Overall, Ukraine's current economic policy mix is likely to disrupt its ability to defend itself against the Russian invasion. It could deepen, rather than mitigate, the crisis facing Ukrainian workers and consumers. Ukraine's global community of friends needs to engage in dialogue with Ukrainians on these issues, including not only government representatives but also civil society and trade unions. At the center of this discussion should be the recognition that building well-funded, democratic institutions through progressive taxation provides the vital link between Ukraine's current need to organize a successful war effort, and its future prosperity in the postwar period.

Luke Cooper

P.S.

The American Prospect

https://prospect.org/world/2023-01-30-ukraine-neoliberal-war-mobilization/