

# Ukraine and the IMF program

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## A short comment on...

- Exchange rate policy:

*Is flexible exchange rate appropriate for Ukraine?*

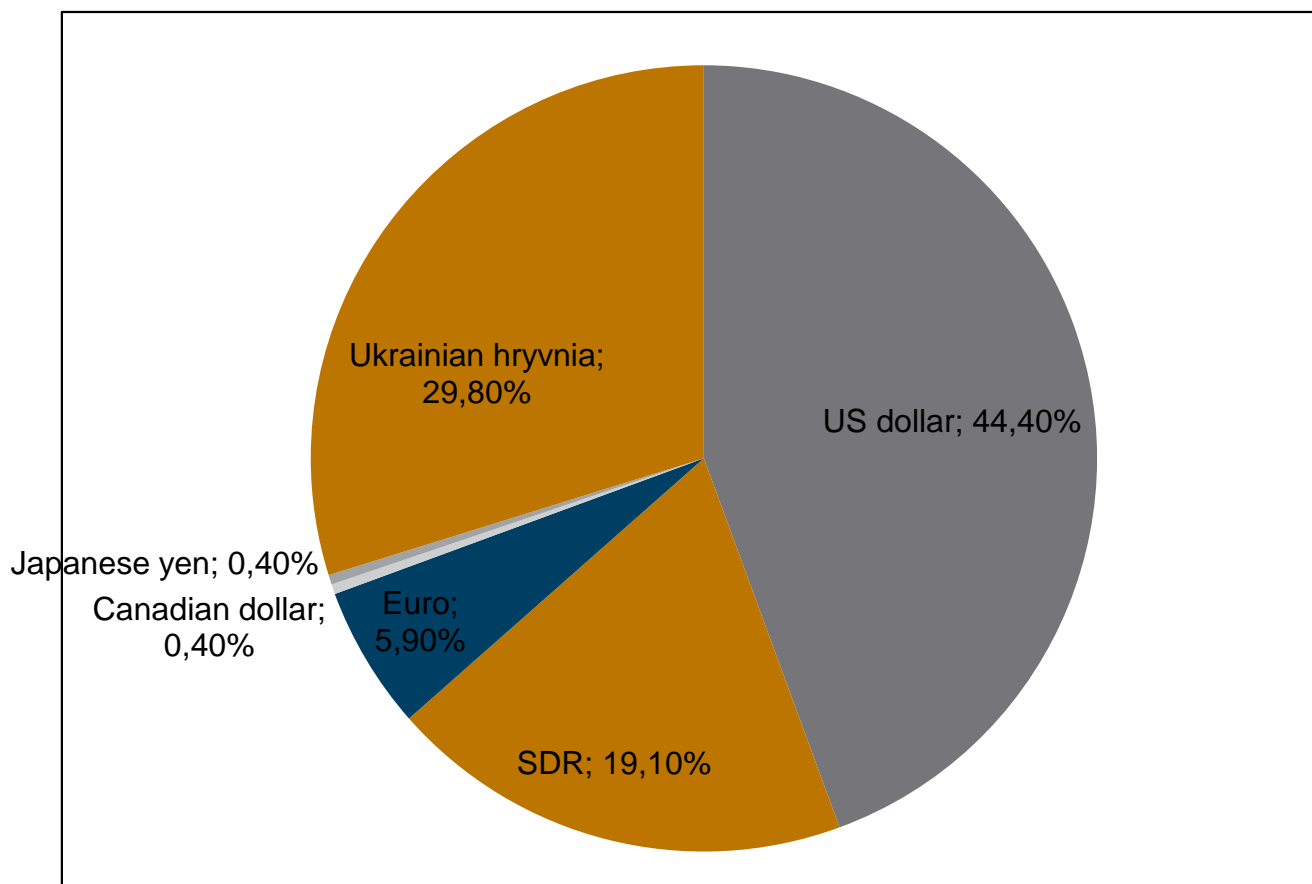
- Fiscal policy:

*Is economic recession a right time to pursue fiscal austerity?*

# Why exchange rate matters

- ‘Small open economy’
  - exports & imports of goods & services = 114% of GDP
- Direct impact on banking sector stability...
  - more than half of all loans denominated in foreign currency
- ... and the burden of public debt
  - 70% of public debt denominated in foreign currency

# Currency composition of public debt end of 2015

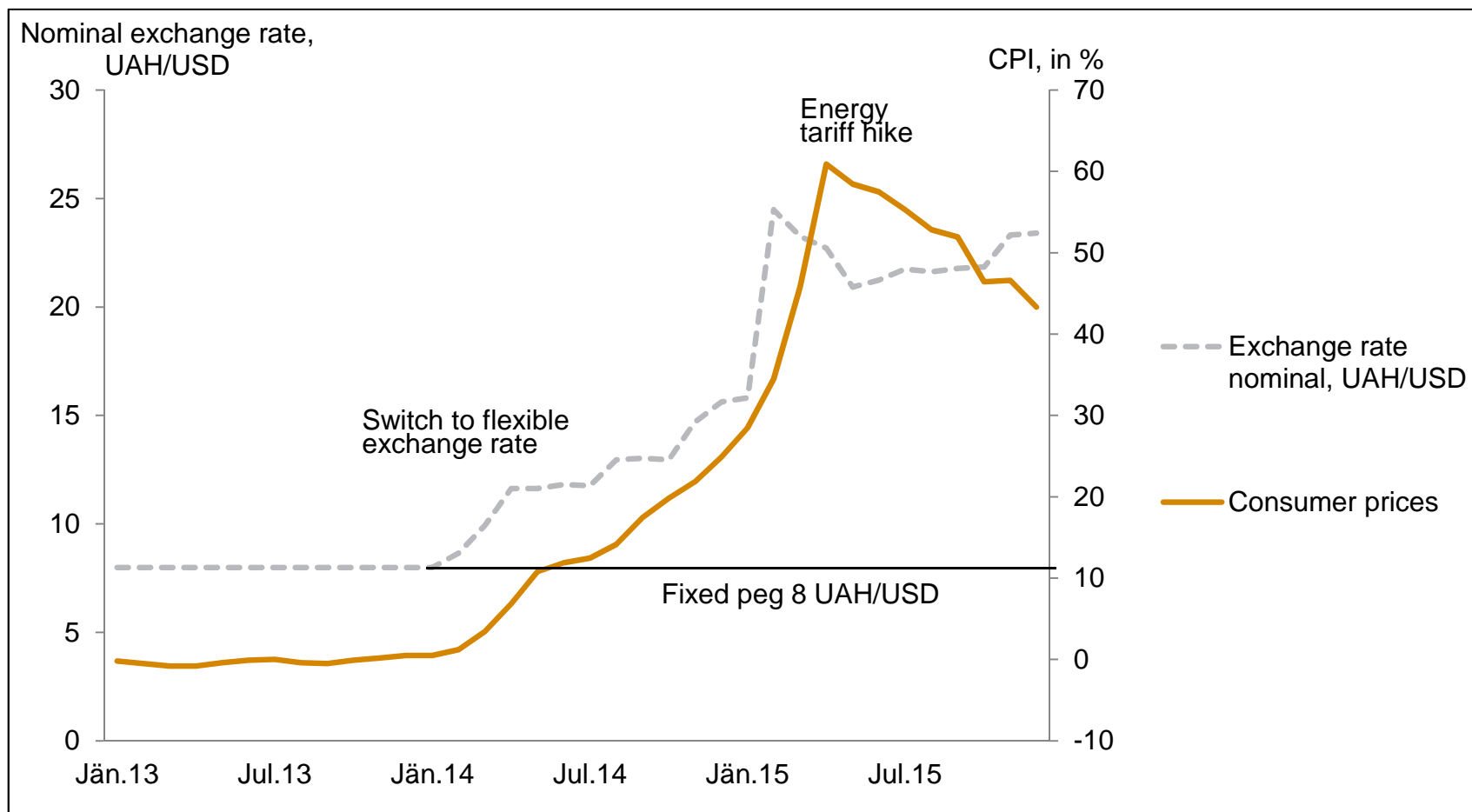


Source: Ministry of Finance.

# Conditions for flexible exchange rate/inflation targeting

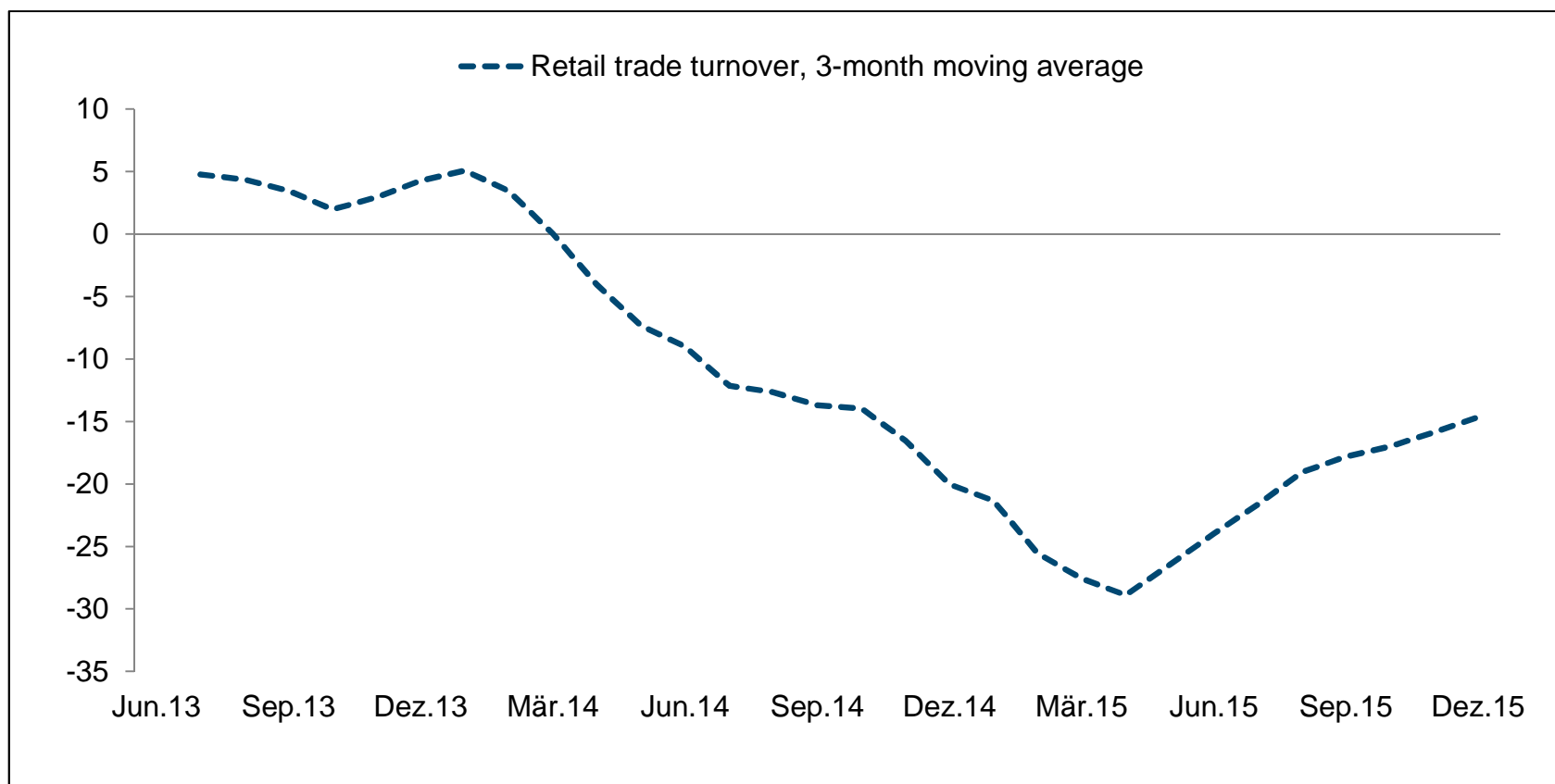
	Present in Ukraine?
'Deep' and liquid market for foreign exchange	No
Effectiveness of 'classical' monetary policy tools: interest rates and open market operations	No
Alternative 'monetary anchor'	No
Reasonable (and credible!) inflation target	No

# Currency depreciation fuelled inflation ...

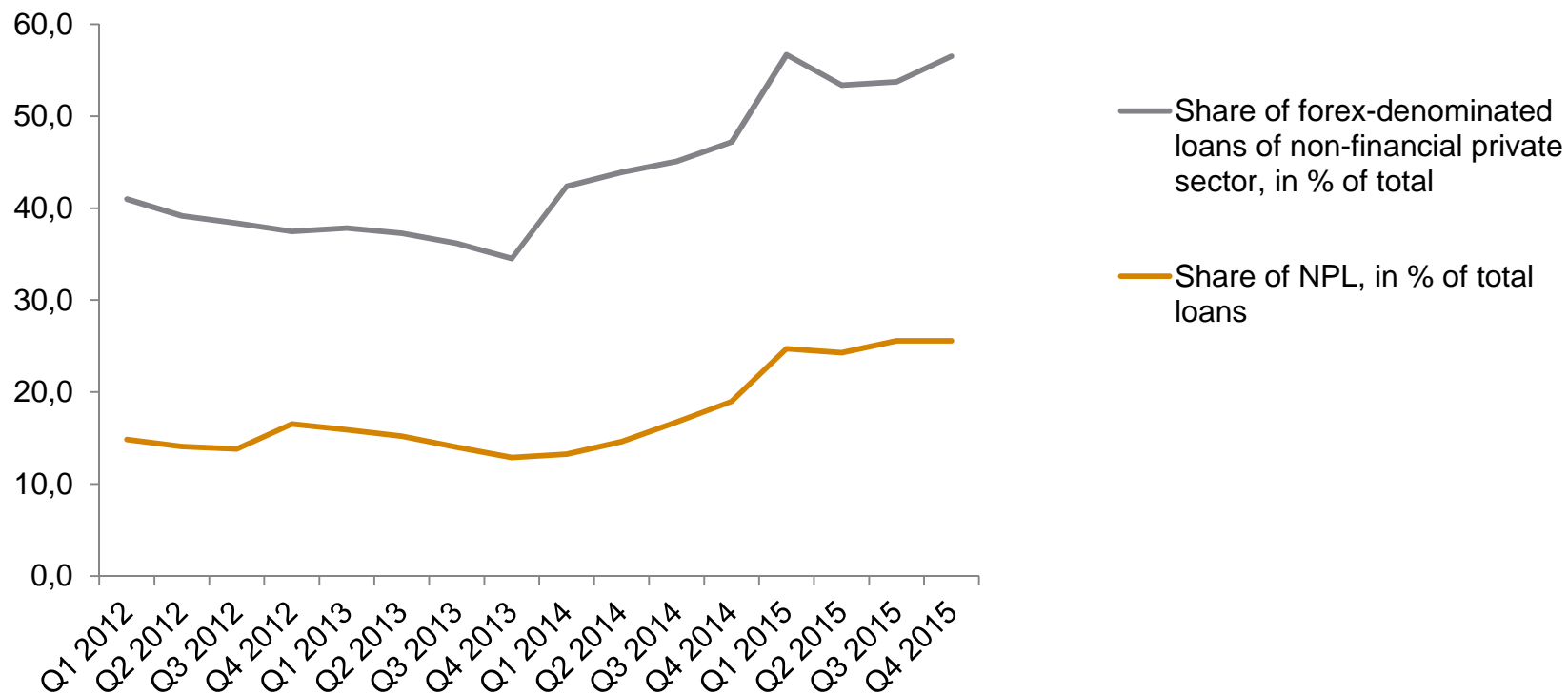


Source: wiiw Monthly Database incorporating national statistics.

# ... which eroded purchasing power of households



# Share of forex-denominated loans vs. non-performing loans

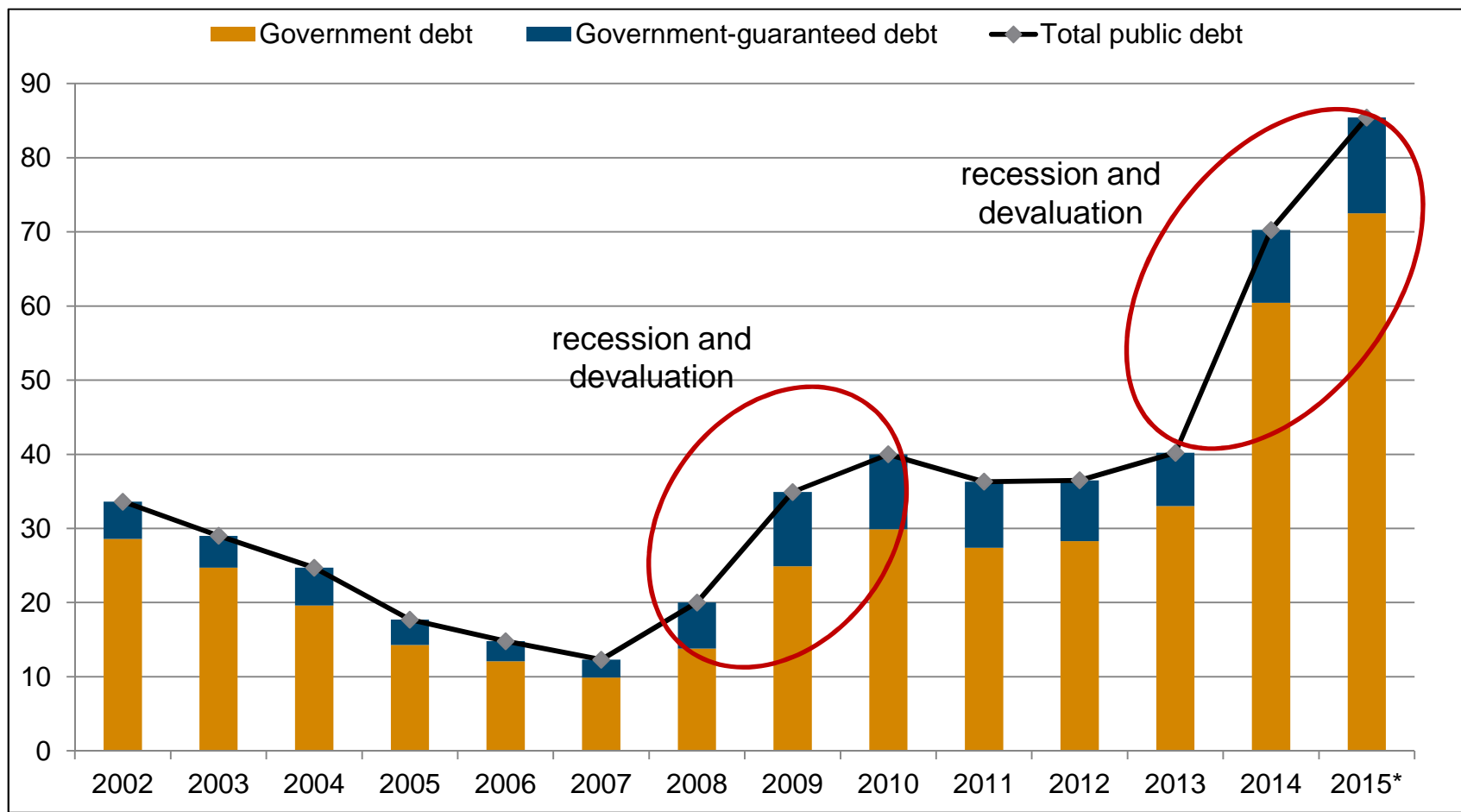


Source: National Bank of Ukraine.



# Public debt, 2002-2015

as % of GDP



\* Estimate

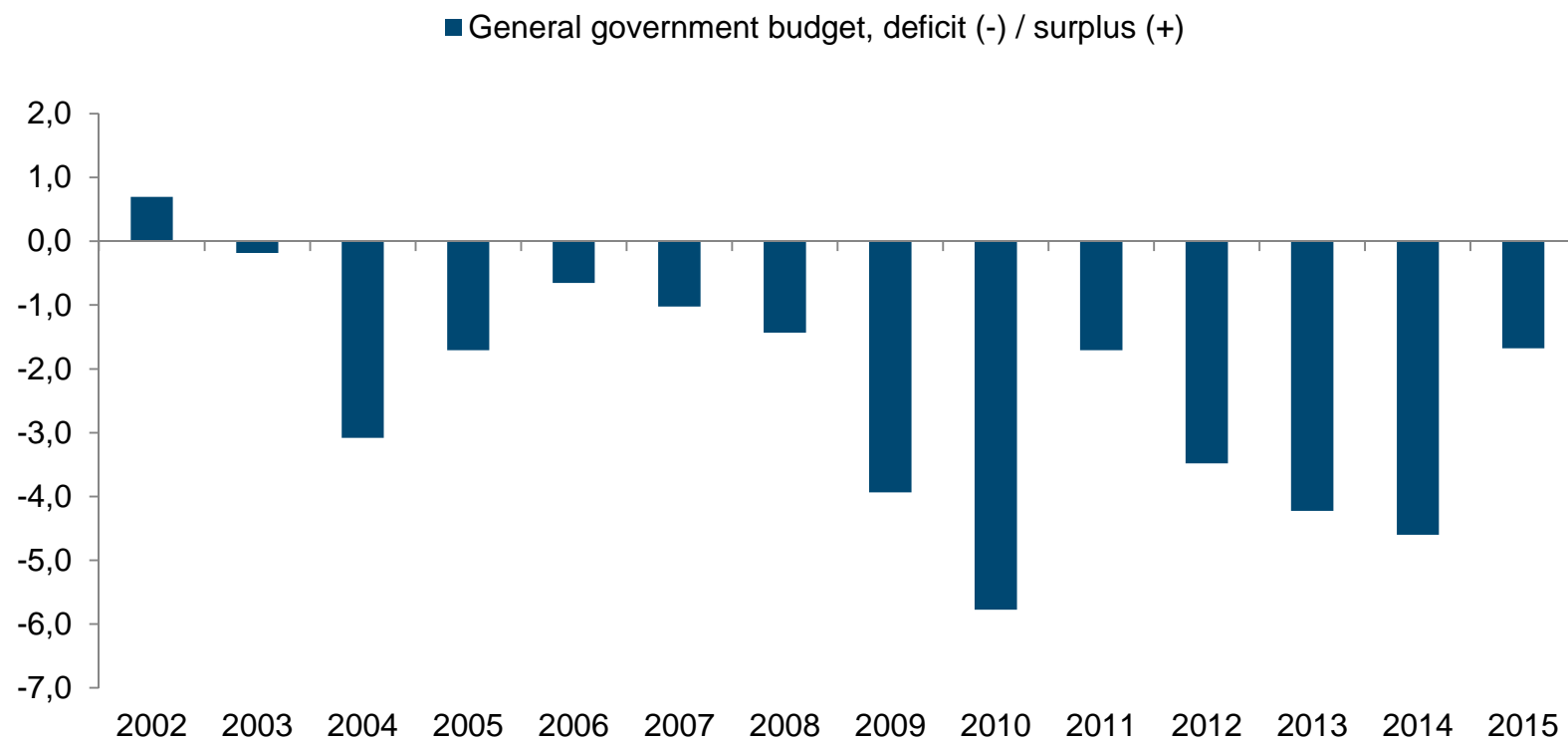
Source: Ministry of Finance.

## Some conclusions

- Fixed exchange rate at 8 UAH/USD under Yanukovych was not sustainable
- Downward adjustment was needed
- But: flexible exchange rate led to excessive depreciation and ultimately extensive capital controls
- A better alternative would be some degree of ER fixation
- For that: substantial forex reserves are needed!

# Budget deficit, 2002-2015

% of GDP



2015: estimate

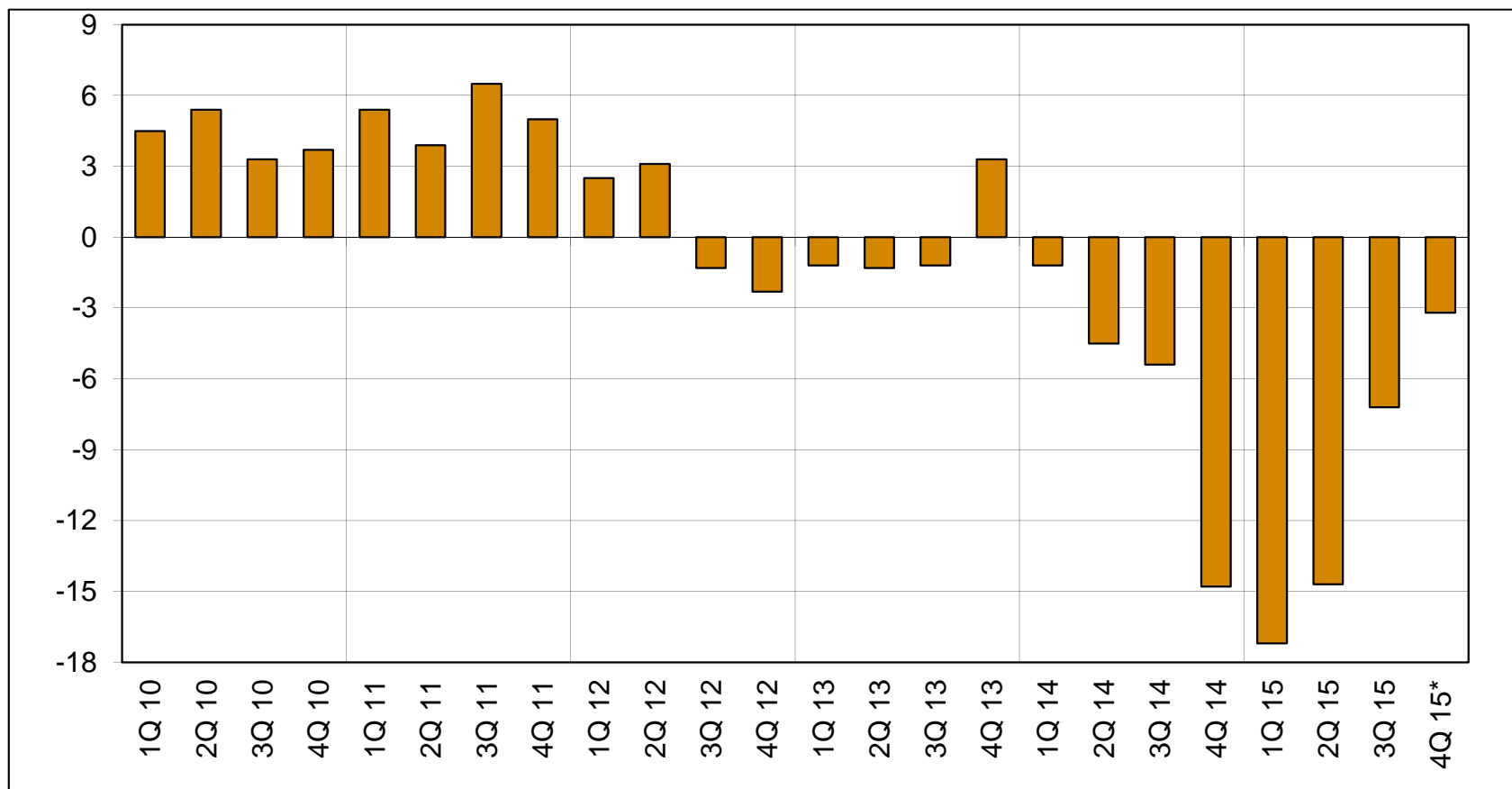
Source: wiiw Annual Database incorporating national statistics.

## IMF-imposed fiscal austerity

- 2014: even keeping budget deficit constant at 4% of GDP required a sizeable consolidation effort because of recession (automatic stabilizers!)
- 2015: budget deficit was *reduced* by 3 pp of GDP in spite of even deeper recession
  - public sector wages and pensions largely frozen despite 43% inflation
- Plus: cuts in energy subsidies (some 3 pp of GDP in 2015)

# Real GDP growth

year-on-year change in %

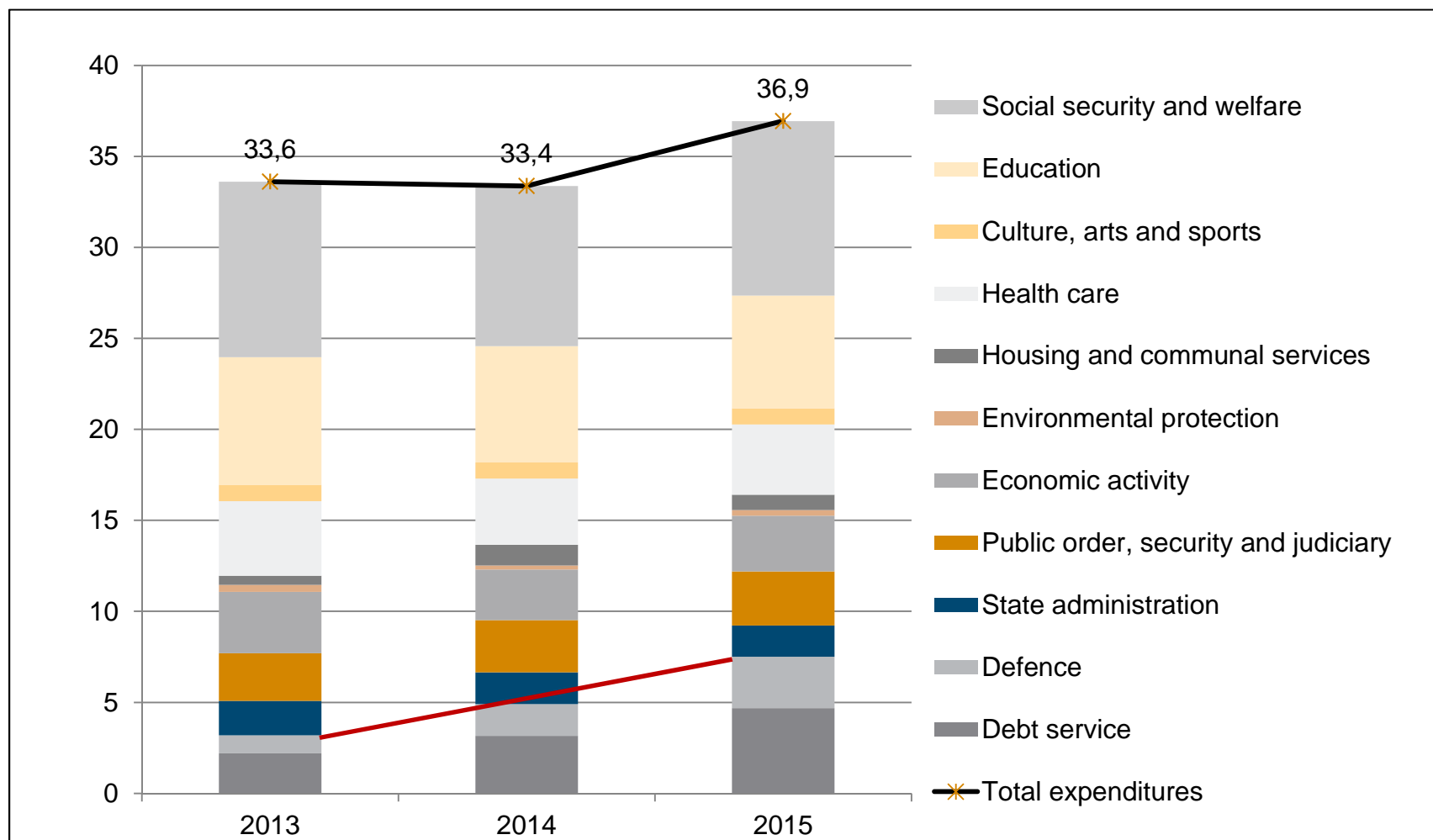


\* preliminary

Note: From 2014 without Crimea and from 2015 without Crimea and parts of Donbass.

Source: State Statistics Service of Ukraine.

# Budget expenditures, as % of GDP



Source: Ministry of Finance.

## Some conclusions

- Fiscal imbalances are **not** at the root of the current crisis (unlike e.g. in Greece)
- Public debt as a share of GDP has risen dramatically, but for other reasons
- Nevertheless: IMF demands pro-cyclical fiscal policy
- Main victims are health, education, pensioners...
- This will likely erode public reform support
- Alternatives: less austerity / change expenditures structure (e.g. more ambitious debt restructuring)

**Thanks for your attention !!!**

**Tipp:**

**„How to Stabilize the Economy of Ukraine“,  
Background study prepared by wiiw, April 2015  
free pdf-download from:  
[www.wiiw.ac.at](http://www.wiiw.ac.at)**