ECONOMIC PROBLEM OF UKRAINE: WHY UKRAINE'S ECONOMY IS IN SUCH A MESS?

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Nowadays we can see that global economy is in trouble and Ukraine's economy has many problems as well. Financial-economic crisis has covered all the country and this situation is spread in all of the regions.

Today the global financial crisis affects the economy of Ukraine through these reasons:

1. Cyclic slowing of global economy in general may reduce demand for exports, and hence export earnings and lead to a decrease in revenue of budget, currency devaluation, reduction of wages, etc.
2. Jumping of commodity prices on world markets caused by the instability of financial and currency markets. In the event of a significant drop problem occurs reduction of trade balance, significantly weaken Ukraine's position in international markets.
3. Quotations collapse in global stock markets led to a sharp and significant drop in shares of domestic companies.
4. Panic in financial markets and the bankruptcy of major investment banks threatened by difficulties in refinancing external debt of domestic banks and corporations.

Ukraine's problems are not just political. In recent weeks its economy has taken a hammering. The government has recently issued short-term debt at interest rates as high as 15%; this year its bonds have done about as badly as Venezuela's. Many analysts are worried that the country will soon default on its debt.

The economic turmoil reflects recent political instability. But Ukraine's economic problems were long in the making. Dodgy economic policy, distaste for reform and endemic corruption have brought the country to its knees.

In the immediate post-Soviet era Ukraine was a massively unproductive economy. Like most former Soviet republics it suffered huge output declines and soaring inflation. But Ukraine was among the hardest hit of the lot. Hyperinflation in the early 1990s resulted from lack of access to financial markets and massive monetary expansion to finance government spending, in the face of sharply declining output. The Ukrainian population was scarred by the experience of hyperinflation. In response, in 1996 the Ukrainian central bank replaced the old currency, the karbovanets, with the hryvnia and pledged to keep it stable in relation to the dollar. The currency continued to wobble through the late 1990s, however, and particularly amid the Russian rouble crisis of 1998.

Both Russia and Ukraine stabilized by the early 2000s. Capital flowed back, attracted in part by relatively high interest rates (the early 2000s, when the Fed pushed its main interest rate down to 1% for an extended period, were a rehearsal of sorts for the post-crisis environment). As foreign cash flooded in the money supply grew rapidly: from 2001 to 2010 broad money increased at an annual rate of 35%. In 2006 and 2007 credit growth averaged 73%. Assets began to look extraordinarily bubbly and high inflation damaged Ukraine's export competitiveness.

After the global crisis, and as the euro crisis intensified, Ukraine suffered from a drought in capital flows (along with much of central and eastern Europe) which placed strong downward pressure on the hryvnia. Protecting the currency drained the central bank's reserves, which tumbled from a high of $40 billion in 2011 to about $12 billion today. Last month the central bank admitted defeat and let the currency go. Currency depreciation, while necessary, will be an economic headache for Ukraine in the short term. About half of its public debt is in foreign currencies: as the hrvynia loses value, Ukraine's debt burden rises. Debt financing has also become more difficult as a result of the Federal Reserve's "taper", which has wrong-footed many emerging markets by stanching the previously steady flow of capital in their direction.

Ukraine has proven reluctant to engage in reform. For a while it felt as if it didn't need to: high commodity prices during the 2000s supported growth. Many of Ukraine's exports went to Russia, a country that was also doing well on the back of high oil prices. But Ukraine was badly hit by the financial crisis and plummeting steel prices. GDP fell by 15% in 2009. That made it a prime candidate for economic streamlining. In 2010 the IMF agreed to loan Ukraine $15 billion—with conditions attached.

Right now Ukraine is not too worried about improving economic management. But big bills are imminent: Ukraine needs to find about $25 billion this year to finance its large current-account deficit and to satisfy foreign creditors.

Multidimensionality of the crisis in Ukraine shows that the depth of the fall of the domestic economy is much higher than similar rates in most countries. This is disparity functioning of the national economy, long-term exacerbation of systemic contradictions:

- compensation of excess consumer demand sustained negative trade balance;
- the dependence of low-tech exports from the world market;
- inefficiency of the financial system and the growth of foreign debt.