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**MANAGEMENT OF THE MODERN MONETARY SYSTEM OF UKRAINE  
DURING THE PERIOD OF MILITARY AGGRESSION****Gvozdej Nataliia***Ph. D. in Economics, Associate Professor**<https://orcid.org/0000-0002-7251-7696>**Department of Finance, accounting and**economic security Pavlo Tychyna**Uman State Pedagogical University, Uman', Ukraine*

*This article analyzes the modern condition of the monetary and credit system, its structure and ways of functioning, as well as indicates problems that prevent the establishment of a stable modern monetary and credit system in Ukraine and proposes solutions. At the moment, Ukraine faces two urgent dangers: war in the country and the rapid devaluation of the Ukrainian hryvnia. External military aggression and the rapid collapse of hryvnia's exchange rate with inflationary pressure in the country leave no opportunity to stabilize or develop the monetary system. Some of the biggest problems also include: "dollarization" of the economy, high corruption levels, limited spread of promissory notes and a low level of monetization. The best prospect for Ukraine is the development of a free trade zone with the European Union, which will enable access of domestic products to the world market. Further opportunities in this area include solving the identified problems by introducing measures to dedollarize the economy, increasing the effectiveness of anti-corruption bodies, developing trade on the open market, supporting the activities of the NBU during martial law and ensuring financial stability and monetization of Ukraine.*

**Key words:** *money and credit system, dedollarization, monetization, corruption, war.*

**Introduction.**

The modern monetary system was formed as a result of a long historical development and adaptation to the needs of the economy. The credit system in general is a set of monetary and financial institutions of a country used by the state to regulate the economy. The credit system serves as a powerful tool for concentration and centralization of capital, facilitating the rapid mobilization of free cash resources and their use in the economy [2]. The extraordinary importance of the role of the monetary system in the country's economy is determined by the breadth of its coverage of various aspects of the activities of the state, economic entities and households in general and ensuring on this basis the continuity of production, exchange, distribution and consumption of tangible and intangible goods, i.e. the process of expanded reproduction. Under such conditions, the analysis of trends in the country's monetary system and the study of the peculiarities of its formation, practical aspects of functioning in the current conditions of the Ukrainian economy is an important area of scientific research [3].

A prerequisite for Ukraine's economic growth is ensuring a high level of development of the national monetary system. The success of its functioning depends on the efficiency of the organization of money circulation in the country, the effectiveness of monetary regulation measures by the central bank of the country and the ability of the banking system of the country to meet the needs of consumers for various financial services; the performance of individual business entities, as well as the country's integration into global reproduction processes. In addition, the



effectiveness of the banking and monetary system depends on the reconstruction of the country's economy in the postwar period and the possibility of normal functioning under martial law, as well as the resource support of economic activities of market participants and the effectiveness of their relations with banking institutions, which creates the basic conditions for sustainable economic growth and improvement of living standards and welfare of the population [1-4].

### **Results.**

Each country has its own peculiarities of the structure and functioning of the credit system, which reflect the specifics of the organization of production, in accordance with certain political and economic conditions. In most countries, the structure of the credit system consists of a banking system and a system of non-bank credit institutions.

An efficient credit system in any market economy requires a two-tiered and hierarchical structure of its institutions. The first tier is the central bank of the country, and the second tier is commercial banks and specialized financial institutions. This organizational structure allows for effective regulation and coordination of activities between different parts of the credit system, which ultimately makes it possible to provide an appropriate level of credit and financial services to meet the different needs of market participants, as well as to distribute operational and administrative regulatory functions between credit institutions and the central bank.

Ukraine has already established a national credit system, which includes the National Bank of Ukraine and a number of credit institutions, including, first of all, banking institutions (the main creditors of the Ukrainian economy) and a set of parbank credit institutions, such as financial companies, pawnshops, and credit unions. Leasing, factoring, and purely credit companies are classified as financial companies under current Ukrainian law.

Today, Ukraine's monetary system is a multi-level mechanism of accumulation and redistribution of finance that needs to be improved. There are problems in the modern financial market that need to be solved by implementing an effective monetary policy and legal regulation. Analyzing them, we can identify several main ones:

1. High level of dollarization of the economy.
2. Not significant spread of bill circulation.

3. 122nd place in the ranking of the most corrupt countries in the world, which leads to alienation of Ukraine in the global market. The new manifestation of corruption in Ukraine is a special kind of corruption - crisis-type corruption, which, on the one hand, is caused by a social crisis, and on the other hand, is the cause of the same crisis, which ultimately makes it impossible to carry out any reform in the country, because it will lose its significance.

4. Low level of monetization of the economy. After the introduction of the national monetary system in 1996, the monetization ratio in 1997 was only 13.5%. As of January 1, 2008, it was 55.8%, and in 2019, there was a sharp decline of 36.1%. Thus, the monetization rate has increased significantly since 2000, but its growth is insufficient. Moreover, due to the war in the country (since 2014) and the devaluation



of the hryvnia, at the beginning of 2021, the level of monetization was 44% of GDP, and at the end of November it was only 38% of GDP. And this is despite the fact that in developed countries the level of monetization of the economy is: in Eastern Europe - at least 30%, the Czech Republic - 79.4%, the United States - 80%, China - 195.3%, Japan - 255.

The main problem for Ukraine's economy has been the war that has been going on since 2014. The full-scale invasion of Ukraine by Russian troops on February 24, 2022, was a major shock. Thus, while the country is being destroyed by military aggression from the outside, a significant collapse of the exchange rate, accompanied by inflationary pressure, has occurred from within.

Based on the identified problems, the following ways can be suggested to solve them and improve the state of the monetary system as a whole:

1. Due to the high level of dollarization of the economy, measures to de-dollarize it should be considered:

- prohibit the setting of prices in foreign currency on the domestic market of Ukraine. In other words, the currency of price and payment should be hryvnia only, and settlements between economic entities should be made in the national currency;
- reducing the devaluation burden on the hryvnia by banning foreign currency lending, which in turn will reduce the demand for foreign currency;
- building confidence in the national currency and stabilizing it;
- introduce high tax rates on the purchase of foreign currency and establish a difference between the purchase and sale rate, with an increase in which the purchase of foreign currency will decrease, as it will not be profitable for short-term investments;
- reduce dependence on foreign creditors and reduce public borrowing.

2. Develop open market operations by increasing bank operations with bills of exchange and spreading bill circulation in general, as well as introducing more forms of securities (shares, bonds, etc.).

3. Increase the effectiveness of anti-corruption bodies in Ukraine, such as the NAPC (National Agency for the Prevention of Corruption), NABU (National Anti-Corruption Bureau of Ukraine), SAP (Specialized Anti-Corruption Prosecutor's Office), etc. In our opinion, some of the most effective methods are

- ensuring inevitable criminal punishment for corruption;
- dismissal from office, followed by a ban on working in public authorities and loss of social guarantees (e.g., pensions);
- to strip MPs of their immunity;
- create transparency systems for people, such as Prozorro;
- annual reporting of government officials.

4. In order to increase the level of monetization, it is necessary to take measures for Ukraine's economic growth, which include the growth of production of goods and services and the development of the national economy.

5. Unfortunately, during martial law, most of the ways to improve the economic situation in the country, including the monetary system, cannot operate at full capacity or do not operate at all (e.g., dedollarization). However, the National Bank



of Ukraine does not stop its work, but rather does everything possible to stabilize the economy as quickly as possible and to provide the most effective assistance to the Armed Forces of Ukraine. The NBU continues to take steps to maintain financial stability in its monetary policy and financial sector regulation. Several of them are worth highlighting:

- ✓ in order to prevent the outflow of capital abroad and to prevent macroeconomic imbalances, the deadlines for settlements in export-import transactions were temporarily reduced from 365 to 90 calendar days starting April 4, 2022. The new requirements will be applied to residents' export and import operations with the expectation that this will expand their capabilities in the face of supply chain disruption due to the war [5];
- ✓ on April 12, the NBU Board decided to make a second repurchase of the government's military domestic government bonds (OVDPs) worth UAH 20 billion. Thus, as of April 13, 2022, the regulator's portfolio of military government bonds already amounted to UAH 40 billion. [6];
- ✓ starting from April 14, 2022, the regulator allowed banks to sell cash foreign currency to the public. It is expected that the resumption of cash foreign currency sales by banks will help reduce opportunities for the functioning of the illegal currency exchange market and reduce risks for citizens;
- ✓ since the beginning of the large-scale armed aggression of the Russian Federation against Ukraine, as of August 22, 2022, more than UAH 20.2 billion in equivalent has been transferred to the military from the special account opened to support the Armed Forces of Ukraine. In particular, UAH 7.2 billion in foreign currency equivalent came from abroad [7];
- ✓ the NBU will continue to support Ukrainian refugees abroad, in particular by creating opportunities to exchange cash hryvnias for the currencies of their host countries.

At the same time, the central bank will finance only critical government expenditures in limited amounts and maintain full transparency in the coverage of such operations. This will help prevent:

- 1) increased fiscal dominance and high inflation;
- 2) weakening confidence in the NBU and unbalancing expectations
- 3) complicating the process of Ukraine's European integration and cooperation with international financial donors [8].

Back in prewar times, the practice of managing Ukraine's financial stability was based on the interconnected use of instruments that support the work of individual sectors (monetary, budgetary, and tax), as well as policy areas (debt, currency, exchange rate, etc.). Today, these instruments are strengthening their work and supporting the state of Ukraine's financial sector and ensuring its resilience to risks.

The main instruments used to support the monetary sector are:

- 1) the key policy rate, which is the main instrument for maintaining the effectiveness of monetary policy and the stability of the monetary sector;
- 2) interest rate corridor for standing facilities, i.e. overnight loans or overnight certificates of deposit, which are available to banks from the NBU
- 3) interventions in the foreign exchange market as an additional tool for



accumulating international reserves, smoothing out excessive exchange rate fluctuations, and supporting the transmission of the key policy rate;

4) other additional instruments, such as mandatory reserves, repurchase agreements, purchase and sale of government securities, and swap transactions;

5) liquidity tenders [9].

Ukraine's current monetary system has its challenges and problems. Inflation is one of the main concerns as it can affect the purchasing power of citizens and the stability of the national currency. The volatility of the hryvnia exchange rate creates uncertainty for businesses and investors.

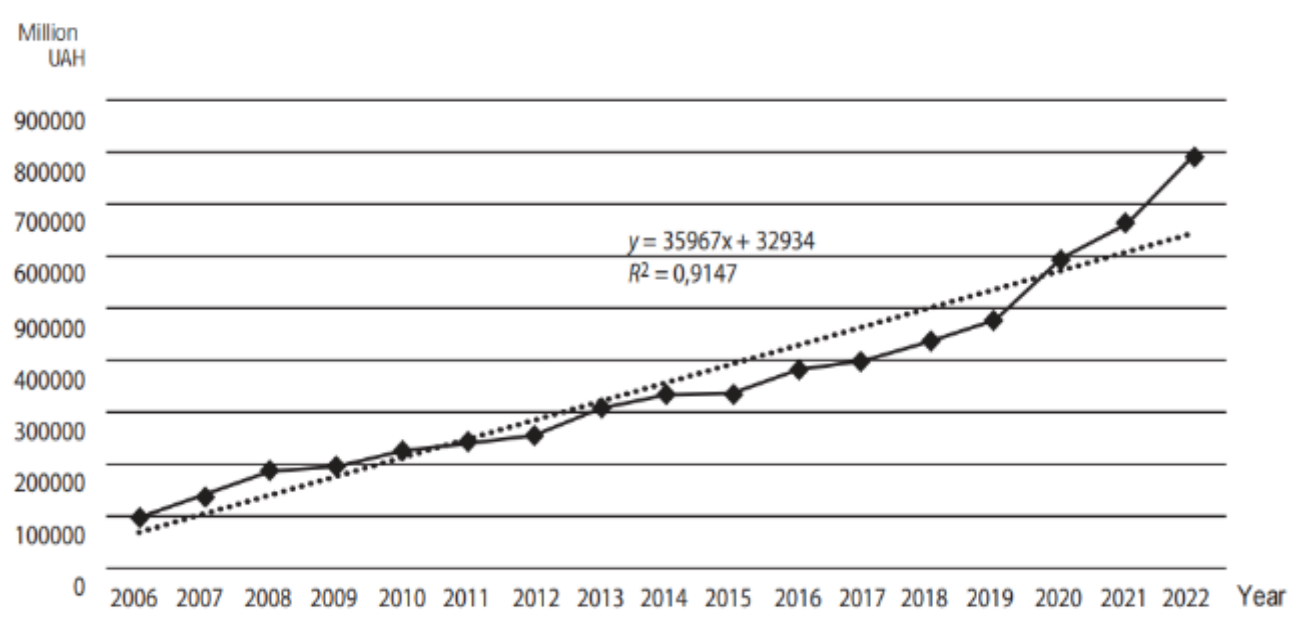
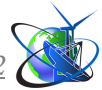
In addition, the system often faces problems of corruption, which can have a vulnerable impact on the financial sector and the general public's trust in the banking system. The banking sector may also face challenges related to poor lending, excessive risk concentration, and lack of transparency.

Economic difficulties and political instability further complicate the functioning of the monetary system, may cause changes in economic strategies, and may affect public perceptions of the stability and efficiency of the system.

Since its independence, Ukraine has already experienced three systemic crises - in 1998-1999, 2008-2009, 2014-2015 - and is currently experiencing the fourth, which is associated with the active phase of the war with Russia. All of Ukraine's systemic crises were accompanied by a decline in production, financial, budgetary, currency, debt and banking shocks. Over the years, the hryvnia has devalued more than 22.5 times, while consumer prices have increased almost 16 times and industrial prices have increased more than 27.5 times. During the crisis of 1998-1999, Ukraine's GDP decreased by 2%, in 2009 - by 14.8%, in 2014-2015 - by 15.8%, and in 2022 - by 31.4% [10]. That is, the current crisis may become the most significant for our monetary system and the economy as a whole. An analysis of the country's monetary base (Fig. 1), i.e. the total of cash issued by the NBU, funds on correspondent accounts, mandatory reserves, funds of other financial corporations, non-financial corporations and households, for the period of analysis 2006-2022 increased more than 8 times - from UAH 97214 million in 2006 to UAH 792537 million as of December 2022.

The key policy rate hike was intended to address the following objectives: to reduce the outflow of hryvnia mass into foreign currency; to increase the time during which the country's economy can rely on international reserves until exports increase; to maintain exchange rate stability and reduce pressure on prices; and to maintain confidence in the hryvnia. Ukraine's medium-term inflation target was set at 5% (for annual growth in the consumer price index) [11].

Most developed countries aim to maintain inflation at the level of 1% to 3% to ensure price stability. For most developing countries, the medium-term inflation target ranges from 4% to 8%, which is higher. In Ukraine, inflation has met the target several times in previous years. For example, in 2011, it was 4.6%, in 2019 - 4.1%, and in 2020 - 5% (see Figure 1). In some periods, inflation significantly exceeded the target level, and was quite high and volatile: in 2000, it was 25.8%, in 2014, 24.9%, and in 2015, 43.3%. In 2022, it reached 26.6%.



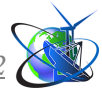
**Fig. 1 Analysis of the monetary base**

It should be noted that when an inflation targeting regime is introduced during periods of high or highly volatile inflation, citizens are distrustful of the new regime and their expectations of the inflation rate change slowly. More realistic inflation expectations can be helped by the effective policy of the NBU as a central bank, which, by setting higher inflation targets with a wide fluctuation band, allows the NBU to achieve its announced goals and strengthen confidence in monetary policy and increase the manageability of inflation expectations.

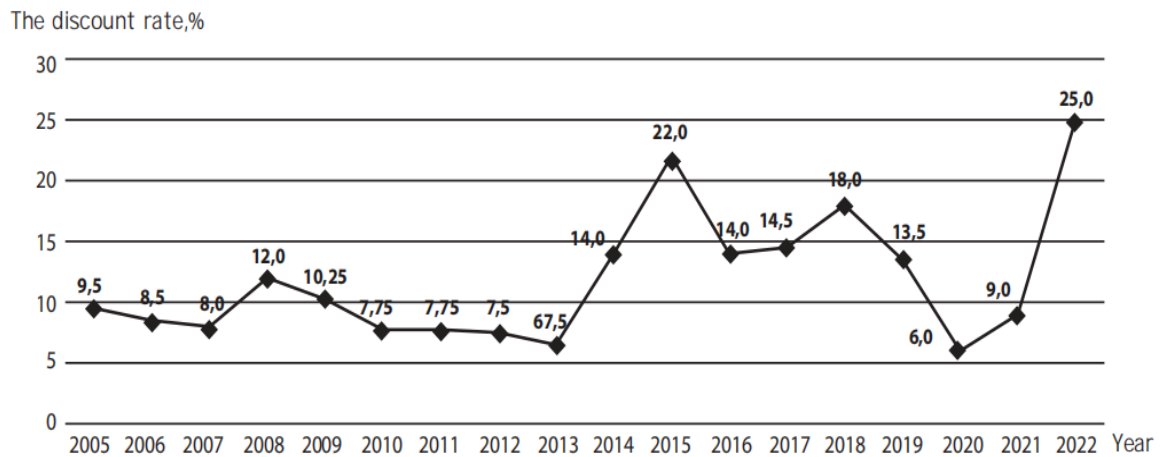
The domestic banking system has always responded sensitively to all crises and other external challenges since Ukraine's independence. Thus, while in 2014 there were 180 banks in the country, in 2015 there were already 163 banks, and in 2016 there were 117 banks, i.e. 63 banking institutions or 38% were liquidated in two years. The downward trend in the number of banks in Ukraine is still observed - currently, there are 67 banking institutions in Ukraine, which is 5.6% less than in the previous year[12].

Russia's military aggression led to an increase in the NBU's key policy rate from 9% to 25%. The increase in the key policy rate was made in the absence of inflation targeting. Currently, the key policy rate remains the NBU's non-main monetary instrument. The main tool is the sale of foreign exchange reserves to ensure the exchange rate is fixed, but the decrease in the country's foreign exchange reserves in 2014-2015 to support the hryvnia led to a spontaneous collapse. In order to prevent the previous scenario, the NBU raised the key policy rate within the expected inflation rate at the time (Figure 2). The key policy rate hike was intended to address the following objectives: to reduce the outflow of hryvnia mass into foreign currency; to increase the time during which the country's economy could rely on international reserves until exports increased; to maintain exchange rate stability and reduce pressure on prices; and to maintain confidence in the hryvnia.

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**Fig. 2 Inflation rate in Ukraine in 2005-2022**

The analysis of the NBU's funds showed their growth after the beginning of 2022. Thus, in 2022, the NBU's funds increased from UAH 34973 million to UAH 82485 million, which is a 2.4-fold increase[13].

Thus, Ukraine's monetary system is developing in a very difficult environment. Nevertheless, the financial sector continues to operate. International support for Ukraine is growing, providing funding for almost 50% of the state budget, external grants and loans have supported the balance of payments and ensured the growth of international reserves, and the NBU maintains its presence in the foreign exchange market. Significant public spending on payments to the military and those affected by the war strengthened household incomes and compensated for the significant decline in private sector spending. The liquidity of domestic banks declined, but remained at a fairly high level.

In addition, the NBU's activities to ensure stability and regulation of Ukraine's financial and credit system in this difficult time can be implemented in the following areas: removing insolvent banks from the market to improve the banking sector; returning to the postwar inflation targeting policy; and ensuring inflationary stability. A system of measures aimed at economic recovery and overall economic stabilization, increasing confidence in the banking sector and the efficiency of the NBU's activities in controlling and regulating the banking system, and ensuring the development of Ukraine's banking system in the future should also be implemented. In particular, monetary policy tools may be used to manage the level of lending interest rates; introduce targeted incentives (e.g., aimed at restoring the real economy) for banks' lending activities; and ease the requirements for regulating lending activities. The measures to be implemented should be aimed primarily at expanding the supply of money to critical segments of the real economy and public finances.



## Summary and conclusions.

Thus, having analyzed the monetary system of Ukraine, we can conclude that it has been actively changing in recent years: a two-tier banking system is being created and developed, and the activities of non-bank credit institutions and independent commercial banks are increasing. In the long term, after our victory, the best opportunity for Ukraine's stable economic development is the creation of a free trade area with the EU and its development. This will ensure improvement of the current customs and tariff legislation of Ukraine and enhancement of the quality of domestic products and their access to the global market. One of the main tasks is to create a transparent mechanism of monetary policy, which will directly affect the efficiency of its development. The prospect of further research is to identify the problems that reduce the efficiency of the monetary system of Ukraine and to develop proposals for their elimination in compliance with the legislatively defined target priorities.

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