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## FOREIGN EXCHANGE MARKET ANALYSIS IN UKRAINE

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### **Abstract.**

One of the factors of economic condition of the country that has a significant impact on economic growth is considered. The exchange rate is a means of implementing monetary policy, with the national currency having limited convertibility as it is not in constant demand in the global financial arenas. Ukraine is undergoing processes of integration into the European Union and development of cooperation with the leading countries of the world, which first of all requires the state to reform approaches to regulation of the foreign exchange market, to search for effective mechanisms and instruments for its implementation, neglecting which causes the currency crises, destabilizes the national currency.

**Key words:** currency market, exchange rate, currency regulation, currency interventions, shadowing.

## **1. Introduction**

At present, many works of domestic scientists are devoted to the interpretation of the concept of "currency regulation". However, in our opinion the most complete definition is V.V. Klimenko, who viewed currency regulation from two sides. On the one hand, these are regulatory acts aimed at regulating capital flows from country to country, and on the other hand, part of the macroeconomic policy of the state, which concerns the sphere of monetary and financial relations of citizens of the country [3].

The currency market is an economic category that can be interpreted from different sides. First, it is a set of relationships that allow the purchase and sale of foreign currency and other currency values. Second, it is the set of specific institutions through which these foreign exchange transactions are carried out. Thirdly, it is the official financial center, that is, the place where currency transactions are carried out [2].

## **2. Presentation of the main research material**

Monetary relations cause significant impact on the dynamics of economic development of each country. Ukraine's economy is characterized by high transparency and highly sensitive to changes in the international environment. To avoid or minimize the negative consequences of financial crises or other adverse factors of external influence in the country are subject to a number of regulatory measures, aimed at defining the conditions of organization and implementation of monetary relations, the domestic foreign exchange market and its actors. In addition to processes occurring in international markets, especially foreign exchange regulation determined by the state, conditions, and direction of internal economic development

of the state. Because currency control is a component both monetary and economic policy of the country as a whole, it is developed and implemented in accordance with national goals [1, p. 80].

In accordance with the innovation law of Ukraine "On currency and currency transactions" (Act), which replaced the Decree of the Cabinet of Ministers "On system of currency regulation" from 1993. As a consequence, the Resolution of the NBU dated 05 Feb 2019 No. 31 repealed obsolete 252 legal acts of the NBU in the sphere of currency regulation. However, on June 20, 2019 there is a norm which obliges to sell 30% of foreign exchange earnings on the interbank foreign exchange market. For SMEs and large businesses, such changes could entail the active use of derivative financial instruments (forwards, futures, options, swaps). Taking into account the forecast, the bankers hope to improve: businesses will increasingly have currency in Ukraine, for now, to withdraw the currency in any time.

On May 8, 2019, the NBU Resolution №66 of May 7, 2019, "On Amendments to the Regulation on Measures to Protect and Determine the Procedure for Performing Individual Transactions in Foreign Currency" came into force [9].

Analyzing the main reasons for the depreciation of the national currency against the foreign currency, first of all, it should be noted that Ukraine is a commodity economy, so its GDP depends, first of all, on the level of external prices in the main export directions (metal, ore, grain). Given that the agricultural sector is still profitable, hostilities in the east, where a significant proportion of mining and machine-building industries are located, have led to a significant reduction in export earnings, which in turn has led to a shortage of foreign exchange in the foreign exchange market Of Ukraine. To the list of factors that contributed to the UAH devaluation should be added such as: negative business expectations, a decrease in foreign direct investment inflows, a significant increase in public debt service costs, devaluation of currencies of trading partners, etc. [7, p. 10].

Taking into account "sharpening political events" in the Ukrainian currency market, it became a turning point in 2014, when the national currency began to sharply depreciate. Thus, at the end of 2013, of UAH exchange rate against the USA dollar on the interbank foreign exchange market

was at the level of UAH 8.11. for \$ USA. In 2015, for the period January - March the rate increased from 15.77 UAH / 1 USA. US \$ 23.44 / \$ 1 USA; in 2016 for the same period - increases from 24,00 UAH / 1 USA. To 26,22 UAH / 1 USA ; in 2017, the peak period was October - December, which was marked by an increase in the rate from 26.52 UAH / 1 USD. US \$ 28.07 / 1 USA; the only summer period of sharp increase in the rate was 2018, when in July - September the rate increased from 26.19 UAH / 1 USA. To 28.30 UAH / 1 USA The USA, which is the result of a currency shortage due to the decline in export activity of domestic enterprises, usually in the winter.

As of March 31, 2019 the official UAH to US dollar exchange rate was UAH 27.25 / USD 1. however, for the period of December 2019, the rate was submitted daily but at the end of the month it increased to 23.68 UAH / 1 USD. USA. Therefore, compared to 2014 and 2019, the UAH depreciated by 2.5 times against the US dollar. The official UAH exchange rate against the euro was 30.57 UAH / 1 euro.

According to statistics, the share of the shadow economy of Ukraine is about 50%, although the real data are much higher. Shadowing the economy is linked to the prosperity of the "black currency market". Currently, several UAH exchange rates have been formed in the country at the moment - the official one that establishes the NBU, the interbank and the so-called "black" (which involves currency trading in the illegal exchange market). In 2014 in Ukraine it was difficult to buy the currency legally, but there were no particular problems with its purchase from speculators. Of course, the currency price in such conditions is much higher than the official NBU rate. Despite this, the official market turnover is falling and the shadow market is rising. Over the last year, the volume of interbank trading, as a rule, does not exceed \$ 300-500 million. per day, whereas before the 2014 crisis, the daily trading volume on the interbank exchange market was about \$ 1 billion [10].

It should also be noted that the "unfavorable" situation in the East, which implies political instability within the country and the ambiguous attitude of the leading countries of the world to the conflict, has a significant impact on the fall of the national currency.

The National Bank of Ukraine used currency intervention from the main instruments, which

was observed from 2015 - 2019, which was a significant predominance of currency purchases over sales volumes (starting from 2016, the use of foreign exchange interventions is aimed at increasing the reserves of foreign currency reserves and increasing the sale of foreign currency). We invite you to pay attention to the recent years the volumes of currency interventions that were carried out by NBU Table 1 and information about the NBU currency interventions by months Fig. 1.

Table 1. Volumes of currency interventions of the National Bank of Ukraine 2014 - 2020 [6]

NBU Currency Intervention Volume by Year (Million USD)			
Year	Sale	Purchase	Balance (sale - purchase)
2014	4579,0	9,3	-4569,7
2015	218,2	430,0	211,8
2016	268,0	503,1	235,1
2017	462,8	272,0	-190,8
2018	1801,82	3173,78	-1371.96
2019	529,23	8462,60	-7933.37
2020	30,00	298,00	-268.00

For the 1st quarter. In 2019, the sale of foreign exchange interventions amounted to \$ 166.8 million. And the purchase - \$ 791.6 million. USD, which amounted to a positive balance of \$ 624.8 million. USA.

According to the Currency Intervention Strategy 2016-2020, the National Bank of Ukraine did not buy currency during the period of fluctuations towards the depreciation of the UAH, and replenished international reserves only under favorable conditions in the foreign exchange market. At the same time, starting in April 2018, the NBU is constantly announcing the volume of foreign currency purchases to replenish international reserves in order to increase the transparency of monetary policy. Due to the new Law on Currency and Currency Transactions, the National Bank is trying to increase the level of foreign investments.

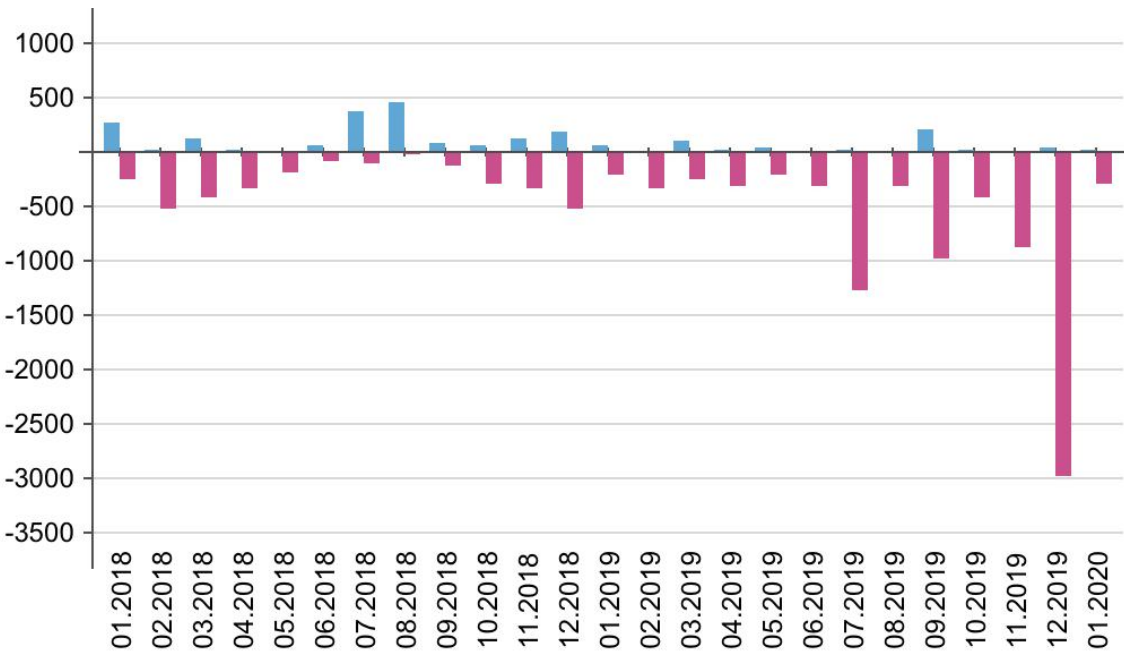


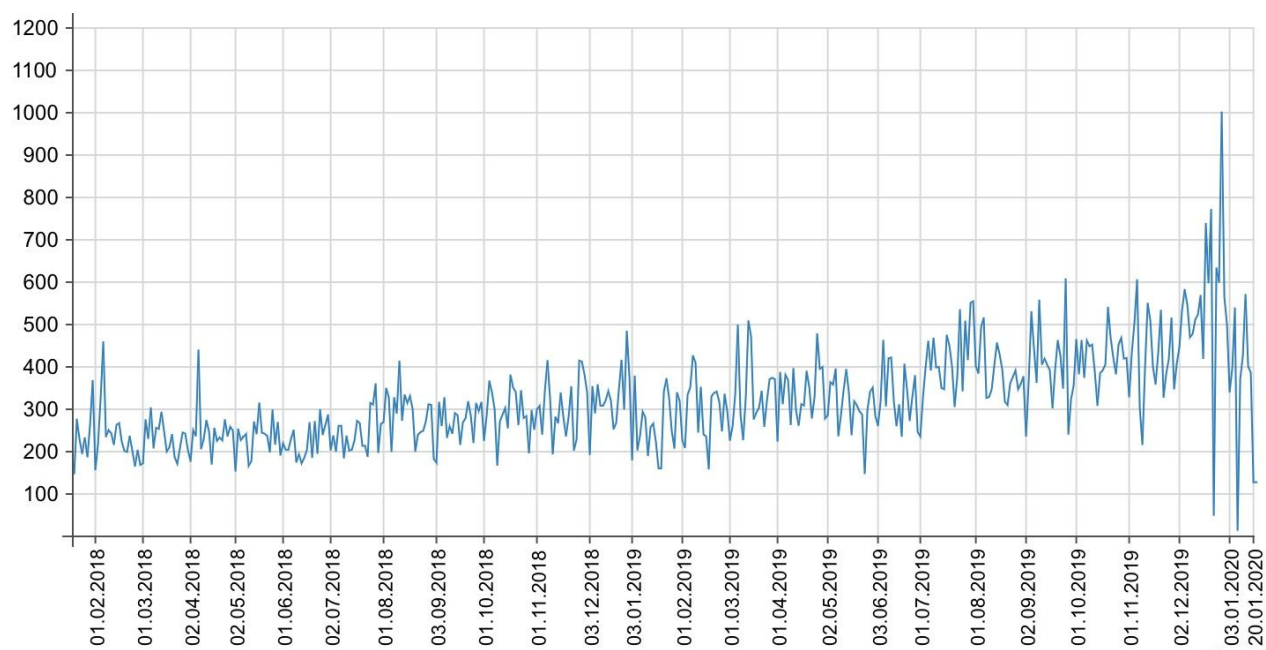
Fig. 1. Currency interventions by months 2018 - 2020 (functionally of Matching) [6]

However, today, given the need to minimize the impact of the regulator on the direction of the exchange rate trend, priority is given to those forms of intervention during which the National Bank does not offer but accepts the price offered by other participants in the foreign exchange market. Forms of intervention in which the National Bank acts as a price-taker are a currency auction and best-rate interventions.

Since April 2018, the National Bank has moved to the implementation of currency interventions at the best and the only rate using Matching, a new functionality for transactions in

trading information systems (Bloomberg, Thomson Reuters). The advantages of Matching functionality (anonymity, unlimited number of participants, promptness) create conditions for more market, transparent and accurate determination of the UAH exchange rate on the interbank foreign exchange market [6].

According to the results of the study of changes in the volume of currency sales on the interbank market over 2 years, it reflects stable dynamics (Fig. 2), but it is unfavorable for the development of the economy, the population is now afraid for what time the national currency will not depreciate, and on the other hand - the inflow will be due to earnings. In December, the sources of currency inflows were traditional export-oriented industries (including agro-industrial complex, metallurgy and mining), portfolio investments and a significant supply of cash currency. Considering the significant predominance of the currency supply over the demand for it and the fact that the UAH strengthening factors are fundamental, not situational.



**Fig. 2. Currency sales on the interbank market 2018-2020, mln. USD USA [8]**

The constant redemption of foreign currency from the market in the context of foreign trade deficit and the current account will cause an upward trend in the dynamics of changes in exchange rates over a long period. This is evidenced by the increase in the average weighted



exchange rate of foreign currency purchase, which may lead to an increase in the devaluation expectations of business and the population, for which such behavior of the central bank in the issue of foreign currency purchase may be an appropriate signal and the formation of foreign currency reserves in Ukraine is not stable.

## **Conclusions**

There are real tendencies of UAH devaluation, which are able to increase inflationary pressure on the national currency of Ukraine. Risks of the NBU's Currency Intervention Strategy to achieve price stability of the Ukrainian UAH require additional analysis and control. But not all scientists agree.

In scientific research, it is possible to trace the opposite views on the optimal exchange rate regime in the current environment. Some advocate the introduction of a free floating exchange rate, while others deny any fluctuations in the UAH price, since they state that they cause losses to the state's economy. Makarenko argues that from the long-term prospects of economic development, the NBU's decision to switch to the UAH exchange rate is a positive phenomenon, the effectiveness of which will in the future depend on the subsequent developments in Ukraine's political arena [5]. T. Kovalchuk, Member of the Board of the National Bank of Ukraine, Honored Worker of Science and Technology of Ukraine expressed another opinion. According to him, Ukraine does not meet the criteria of an efficient market economy, which is a prerequisite for the transition to a regime of floating exchange rate [4].

Therefore, the country first needs to pay attention to the key problems that affect the exchange rate. After all, issues related to the formation of the "black currency market", the shadow economy, dollarization of the economy, currency speculation, above all unstable political situation, high debt load on the country's budget, find the optimal exchange rate regime, improve the legislative base, establish transparent and rational rules for international activity.

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