

ICPS newsletter®

The global financial crisis hits the hryvnia

The hryvnia is likely to continue to devalue over the next while, writes International Centre for Policy Studies economist Oleksandr Zholud in an article for Gazeta po-Ukrainski, a newspaper. The reasons for this are several: the foreign trade deficit is rising in Ukraine, external debts need to be serviced by the private sector—especially banks—, prices are falling on steel markets, and the latest jump in natural gas prices is due at the beginning of 2009. The financial shakedown in September has also had its impact

The crisis in the mortgage sector hit the financial system

At the beginning of 2008, Wall Street, the world's main stock platform, listed five investment banks: Bear Stearns, Lehman Brothers, Merrill Lynch, Morgan Stanley and Goldman Sachs. This kind of bank is not involved in holding deposits and issuing credits, as commercial banks do. Instead, they directly buy stocks and bonds in corporations, form portfolios out of these, and then sell of stakes or trade the securities in their portfolios. Typically, they also provide consulting services for the preparation of mergers and acquisitions (M&As), act as guarantors when stock is issued, and so on.

The total assets of the Five at the beginning of this year were valued at over US \$4 trillion. This was about 26 times more than the current value of Ukraine's entire banking system. The subprime mortgage lending crisis that began to unfold in August 2007 hit the entire financial system badly, affecting even investment banks. Massive debt write-offs began, while the banks' own stock fell sharply in value.

The first to collapse was Bear Stearns. In March 2008, it was bought out by JP Morgan for US \$2.2bn, on condition that the US Federal Reserve gave Bear Stearns US \$30bn to cover bad debts, that is, those what were unlikely to be paid in time or in full. The bank was bought at US \$10 a share, although at the beginning of 2007, its stock was worth 17 times more.

On 14 September, Lehman Brothers announced that they were filing for bankruptcy with the courts, while Merrill Lynch sold to the Bank of America for US \$50bn that same day. When the market lost three of its five investment banks, pressure on the two that remained grew fierce. On 21 September, Goldman Sachs and Morgan Stanley were forced to register with commercial banks. As of now, these two financial institutions can borrow from the Fed should the need arise.

Shockwaves on US markets reverberated around the world

Steep fluctuations on US stock and commodity exchanges, the bankruptcy, sell-offs and changes of status of the largest investment banks affected the entire world's financial markets. They hit Ukraine and Russia as well. The collapse of share values in both countries was far more significant than in the US or Western Europe.

Indeed, it has affected the hryvnia exchange rate. On 16 September, the US dollar rose UAH 0.045 on the Ukrainian interbank currency market. The following day, it rose another UAH 0.115, and on the third day, it rose a further UAH 0.075. This was spurred largely by growing demand for the currency, especially on the part of non-residents. Altogether, in three days the interbank increased the dollar rate above the official UAH 4.85 and broke the UAH 5.00 barrier. The following week, the dollar continued to grow and went beyond the official corridor set for 2008: UAH 4.85 ±4%, that is, UAH 5.044/USD.

By the way...

On 30 September, the Centre's economists completed work on the latest issue of *quarterly predictions*, which analyzes the situation in the main sectors of the economy, government policy and its impact on the economic situation.

Under the "Fostering legislative support for gender parity in Ukraine" project, a collection of analytical papers and bills was published, called "Current issues in gender parity in Ukraine."

Newsletter editor Olha L'vova participated in the Alexander Kwasniewski Summer Academy on European Integration in Poland 23–28 September.

Under the "Managing Migration in the Black Sea Region: Improving the implementation of national policy in Ukraine, Moldova and Romania through regional cooperation among NGOs" project, the Centre's experts drafted an analytical report on national migration policy.

Participating analysts in both the government and non-government sectors were selected for the "Ukrainian-Polish policy analysis internship program" project. These individuals will gain experience in preparing solid analytical papers and a certain amount of recognition in their fields.

At the moment, the National Bank of Ukraine has not intervened on the currency market and has not increased its volume of credit issues. The question of how managed the hryvnia exchange rate is remains open. ■

For additional information, contact ICPS economist Oleksandr Zholud by phone at (38044) 272-1050 or via e-mail at ozholud@icps.kiev.ua.

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icps newsletter editor Olha Lvova (olvova@icps.kiev.ua). Phone: (380-44) 484-4400.

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