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Public Debt: Ukrainian Realities

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Abstract: The paper investigates the public debt and macroeconomic and macro-financial aspects of its development in Ukraine. The assessment of the relationship between the public debt and fiscal indicators is made in the context of financial stability and sustainability. The relationship of the public debt and monetary indicators and its impact on inflation and price stability in the context of fiscal sustainability and macroeconomic balance are analysed. The causality of public debt is revealed. Dialectic, as well as economic, financial and social, effects of the debt policy are defined. The directions for the debt policy improvement in Ukraine are offered.

Basic Results of the Research

Today, the Ukrainian economy is developing in a complex extraordinary environment of government finance crisis, significant weakening of financial stability and equilibrium, and acute internal and external challenges. Further prospects for macroeconomic and macro-financial stability in Ukraine primarily depend on the ability of the Government to reform the economy and finance, to effectively fight corruption and embezzlement at all levels of public administration. The need for successful solution of these challenges requires decisive actions and appropriate amount of financial resources. In these circumstances, all real sources of funding should be used. But now virtually, the only possible way out of this difficult and highly threatening situation and the best method of covering the financial resource deficit is raising funds through a system of debt finance.

The effective use of public credit really allows the state to survive, to meet the urgent current problems, to balance the needs of the present and future development, expanding the fiscal financial opportunities. However, in recent years, when the involved financial resources were used for current budget expenditures, the increase of borrowing costs in the economic and financial crisis has led to the alarming growth of public debt and the cost for its servicing. All this shows the growing role of debt finance, the important role of the public debt in the economic policy of the state, and its financial security. So, now the urgent task of economic theory and finance practice is to develop a rational policy of public borrowing, which will allow using the potential of debt finance, while minimizing the negative effects of public debt.

The public debt, as a result of debt capital movement in the system of public credit, has now become a permanent, immanent component of government finance and an important tool for a system of macroeconomic regulation. However, in Ukraine in recent years the use of financial resources for current budget expenditures, raising of borrowing costs in times of economic recession and crisis have led to the alarming growth of public debt and the cost for its servicing. All this transformed the public debt into a significant risk factor for macro-financial stability and further development of the country.

The principles of economic nature, the nature and functioning of public credit and public debt have been explored in financial literature to some extent. The works by the representatives of Ukrainian classical school of public finance of mid 19th - early 20th century and by modern national scientists and financiers

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have taken the proper place in this research. Important contribution to the study of these complex problems was made by modern Western economists. However, in the financial literature in general and in our national, in particular, there are scanty works devoted to theoretical and methodological principles of public credit and public debt. Without deep disclosure of these matters it is impossible to explore the theoretical background and nature of public debt and, consequently, to build a sound debt policy. The development of an effective debt policy as an integral part of macroeconomic and institutional mechanism of the state will provide financial stability to promote sustainable economic growth and to minimize the negative impact of external factors. Therefore, research on the public debt and its role in ensuring fiscal sustainability and macro-financial stability is urgent now.

Formation of public debt is an integral part of the economy and an important tool for macro-financial regulation. Qualitative (structural) and quantitative (dynamic) characteristics of debt formation are linked to all macroeconomic and macro-financial processes in the country. According to the dynamics of macroeconomic and macro-financial indicators (for the years of Ukrainian independence) three main stages of national debt formation in Ukraine could be distinguished: 1991-1996 – recession; 1997-2007 – relative macroeconomic stabilization in some segments of the economy and finance; 2008-2015 – financial and economic crisis and post-crisis period.

During 1991-1996 the combination of expansionary fiscal and monetary policies, the existence of high budget deficit and emission financing led to disruption of macroeconomic and macro-financial stability and hyperinflation processes. The debt policy of Ukraine has been formed and focused on meeting the short-term fiscal objectives. Raising funds through loans was carried out without full institutional and legal framework for public credit institution operation. In the debt structure the external debt prevailed. In that period loan securities were issued, which gradually replaced the direct NBU loans for financing the budget deficit. The value of public debt in that period exceeded the optimal limits resulting in excessive servicing costs.

At the stage of relative macroeconomic stabilization in some segments of the economy and finance in 1997-2007 the state debt policy as a whole did not promote sustainable development, but rather adversely affected the social and economic aspects. The continued negative trend of public debt in 1997-1999 under the high cost and short-term of borrowing transformed the public debt into real macroeconomic and macro-financial threat to the development of the country. In 2000, the debt reached a critical point of 60% of GDP. The consequence of this policy was the default of the state on the debt liabilities and foreign currency crisis. The credibility of the state as a fund borrower has been lost for a long time, thus producing a negative effect on selecting investors. After numerous external debt restructurings, the international capital markets happened to be virtually closed to Ukraine. The internal debt crisis limited the Government's possibilities to domestic borrowing, forcing the state to switch to a policy of reducing the debt burden (Vakhnenko T.P.: 2006, p. 262).

During 2001-2007 a tendency was observed to reduce the size of public debt and, consequently, the costs for its servicing dropped, and that could be taken for a positive trend. It should be noted, that the potential of public loans, particularly, their investment component, has hardly ever been used. As a result of giving priority to external borrowing in the structure of external public debt, its share increased year by year, which made the currency risks grow. The market of public loans continued to serve for meeting the only fiscal interests of the Government. The state actually did not use the market instruments, which greatly reduced the effectiveness of fiscal and debt policy.

The irrational and situational debt policy formed significant risks to macro-financial stability in the country in crisis and post-crisis period. This rapid increase in public debt was accompanied by further ineffective use of attracted resources for current needs of the Government. This debt policy has rapidly exhausted the possibilities to mobilize additional financial resources transforming the public debt into the source of risks to fiscal and monetary stability. Synergistic negative effects of public debt and worsening of destructive processes in the economy put the country on the brink of pre-default state in 2014. Only signing the Stand-by Loan Agreement with the IMF for the period of 2 years on April, 30 2014 in the amount of 17 billion dollars and receiving the first two tranches of the IMF loan (3.2 billion and 1.5 billion dollars) enabled the country to finance the key expenditures, avoiding default in 2014. On March 11, 2015 the IMF approved a Stand by Program replacement with a new, four-year Program of "Extended Fund Facility". The first tranche of $ 5 billion dollars within the new Program were received immediately after its adoption. The provision of the second tranche of 1.7 billion dollars, which was fully channelled to replenish the National Bank reserves, was approved by the Board of the IMF Directors on July, 31 2015.

The new Program of cooperation between Ukraine and IMF provides for a number of terms, but all of them somehow are related to implementation of reforms aimed at stabilization of the Ukrainian economy and return it to the path of sustainable economic development. A new Memorandum of Cooperation with the IMF also provides for structural reforms, including the anti-corruption reform, judicial reform, deregulation and improvement of business climate, also the public enterprises' reformation, including "Naftogaz". At the beginning of October 2015 Ukraine received 6.7 billion dollars, then to be sent 2 more tranches of 1.7 billion dollars each. In 2016-2018 it is expected to be provided with 12 tranches of $600 million. Together with the funds from other lenders Ukraine may receive up to 40 billion dollars. The amount of 40 billion dollars for financial assistance emerged as the result of the assessment of Ukraine's needs, and the latter will be covered from three sources: the IMF, funds of other international organizations, and private investors.

Currently, the actual situation cannot be justified specifically with military operations in the temporarily occupied territories, as far as the new Government is required to immediately conduct effective structural and institutional reforms. But the borrowings are still used to finance the budget deficit and repayment public debt service, replenishment of NBU reserves, that is, they are used for current fiscal needs, and that only respites the financial-economic and social problems of the country. Therefore, the urgent task is to channel financial resources borrowed from international organizations and foreign countries for necessary reforms aiming at actual use of debt finance for the needs of sustainable development and achieving macroeconomic and macro-financial stability. Without change in the priorities of the potential use of the public credit system, the debt accumulation will lead to rapid deterioration of the economy and finance.

Risks and threats of increasing public debt are especially manifested in fiscal and monetary plane. We will analyze in detail the role and importance of public debt as a risk factor for fiscal sustainability and macroeconomic stability, and examine its basic parameters in the context of the monetary component of macro-financial stability. The public debt is closely linked with fiscal policy in general and with budget deficit, in particular. The main reason of the public debt growth is the budget deficit. In recent decades, the growth of public expenditures in all developed markets was observed, resulting in agreement that the budgets were with deficits, and the public debt grew. If the budget deficit persists for a long time, steadily increasing public debt, the government's ability in conducting a stabilization policy is reducing. Under such conditions, interest payment on public debt is the main source of the state budget expenditures.

With significant amounts of public debt, its service costs may become the main or even the single reason for the budget deficit. If the GDP is unchanged or reduced, and the budget deficit continues to be financed by public debt increase, it can lead to a situation where tax revenues will not be sufficient to pay the interest on the debt. Therefore, to reduce the ratio of public debt to GDP it is necessary to have the budgetary surplus and excess of economic growth above the real interest rate. These findings are the basis of the theory of fiscal sustainability, which is the basis of current approach to debt policy. Achieving long-term sustainability of public finance is a priority of budget policy. In this case, sustainability is understood as solvency, i.e. the ability of the borrower to service debt avoiding default. The objective of the analysis of fiscal sustainability is to show what the current budget policy should be for the state to remain solvent and liquid in the long term perspective.

Budget constraint plays a key role in public finance assessment, fiscal policy interpretation, and anticipation of some shocks for the budget. It provides that the difference between the state expenditures and revenues is compensated by a corresponding change in the value of the Government debt. The stability of Government finance in the long run depends on the difference between rates on loans and GDP growth. Rates on loans usually exceed the growth rate of the economy. Therefore, to maintain sustainable debt levels, either tax rates should be increased or spending on goods and services and transfers to the private sector should be reduced, which can significantly reduce the positive short-term effects of debt financing.

In domestic practice it is advisable to go to the regular evaluation of the effectiveness of debt policy. Meeting this challenge involves development of clear (quantitative) indicators on the performance of public debt management. One of the methodological approaches that has proved its efficiency and is widely used in the practice of the developed markets is the "target method". According to this approach, by analyzing the situation of national and international financial markets, and taking into account the needs of the state, specific indicators are developed and regularly recorded in a certain period that should be derived from the operations of borrowing and debt management. To determine the allowable size of public debt for the countries with emerging markets the following indicators should be included:

1) the share of public debt relative to GDP, which reflects the stability of public debt; higher level of coefficient ratio of public debt to GDP ratio means increased risks of default in the state due to growing debt servicing costs to GDP;

2) the proportion of foreign currency debt in total public debt, its higher value indicates the risk of potential increase in expenditures for repayment and debt servicing in case of depreciation of national currency (Danilenko A.: 2010, p. 236).

According to the Budget Code of Ukraine, the size of the public debt should not exceed 60% of GDP. In general, the dynamics of the state debt relatively to GDP reflects the stability of public debt and shows the government's ability to service the debt in the short and medium term, based on realistic assessment of economic development and availability of political and social factors that limit the effectiveness of fiscal policy. Setting the constitutional limitations of public debt is the most effective means of preventing political abuse of debt finance. Although its introduction and consolidation in the current political process is problematic as far as the current generation objectively is not interested in establishing strict constitutional barriers that would hinder shifting the debt on future generations, summarizes German professor S. Blankart (Blankart S. : 2000, p. 409).

Table 1

Dynamics of State Debt of Ukraine in 2000 - 2014

Indicator	2000	2002	2004	2006	2008	2010	2012	2014
1 Public debt, bln UAH:	64.2	64.5	67.7	66.1	130.7	323.5	399.2	947.03
internal	20.8	21.4	21.0	16.6	44.7	141.7	190.3	461.00
external	43.4	43.1	46.7	49.5	86.0	181.8	208.9	486.03
2 Guaranteed debt by the state, bln UAH	12.8	11.3	17.7	14.4	58.7	108.8	116.3	153.80
3 Total amount of state debt and guaranteed by the state debt, bln UAH	77.0	75.7	85.4	80.5	189.4	473.1	515.5	1100.83
4 Ratio of the state debt and guaranteed by the state debt of Ukraine to GDP (%)	45.3	33.5	24.7	14.8	20.0	39.9	36.6	70.3

Source: Calculated according to the Ministry of Finance of Ukraine.

During 2000-2007, the increase in nominal public debt was much lower than nominal GDP growth, which enabled to reduce the debt burden. The ratio of public and publicly guaranteed debt to the GDP in Ukraine was shrinking for 2000-2007 from 45.3% of GDP in 2000 to 12.7% of GDP in 2007. By 2007, the ratio of government debt to GDP decreased continuously keeping it at a relatively stable level, on the one hand, and high rates of economic growth – on the other. However, since 2008 the amount of public debt and its ratio to GDP has been increasing because of the unfolding crisis, and, consequently, the increased needs of the state in public borrowing, as well as in connection with the suppression of economic activity.

The ratio of public debt to GDP at the end of 2008 was 20%, and at the end of 2010 – 39.9%. In 2012, because of reduction in economic development and increase of the Government activity the public debt amounted to 36.6% of GDP. In the following years the trend lasted of public debt increase to GDP, which reached 70% in 2014. An important factor for a significant increase in the value of government debt in 2014-2015 years was hryvnia devaluation. Thus, in general, Ukraine's public debt grew from 64.2 to 947 billion UAH in 2000-2014, that is by 14 times. Over the same period, its share in GDP increased from 45% to 70%.

According to our estimates, the share of public debt to GDP will greatly exceed the point of 100% in 2016. The rapid growth of public debt produces a negative effect on all processes of socio-economic development of Ukraine, leading to significant risks for macroeconomic and macro-financial stability of the country. As a result of hryvnia devaluation (from 7.993 USD at the beginning of 2014 to about 15.8 USD at the end of the year) during 2014 the government debt of Ukraine increased by almost twice in UAH equivalent. In terms of GDP drop the ratio of the debt to GDP is worsening, thus, this figure of 2014 significantly exceeds the critical limit, and because of hryvnia devaluation and new borrowing, it is more than 110% of GDP.

The results of our calculations confirm that the budget deficit contributes to the growth of public debt in Ukraine. Thus, the increased service and discharge of the debt requires increasing the value of borrowing and increasing the tax burden; this means that the government borrowing has taken the form of taxes. Based on our calculations through using economic and mathematical modelling, we have determined that the increase in the budget deficit by 1% leads to an increase in debt to 6%, in tax revenues – to 0.66%, increase in spending on servicing and debt repayment – to 7.38% , resulting in an increase in the budget deficit additionally by 0.078%. Under such circumstances, to pay off the public debt and interest payments, ever bigger proportion of state budget revenues and GDP is channelled. Thus, we estimate that about 40% of the state budget in Ukraine is aimed to pay off public debt and interest payments in recent years, which practically means reduction of public goods and services' financing (Fig. 1). The analysis allows us to conclude that the national debt is now generating considerable risks to fiscal stability of the country. Significant amounts of borrowings under financial, economic and social recession further exacerbates the threats and risks to macro-financial stability in the country.

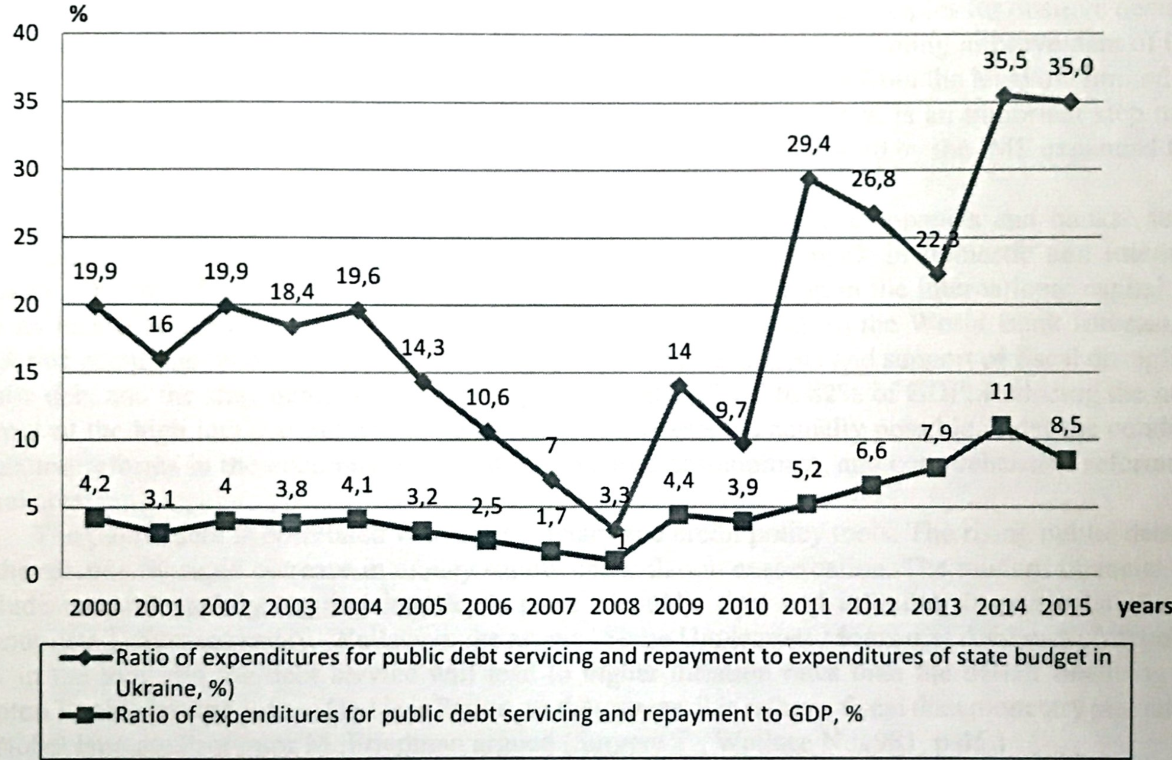

Fig. 1. Dynamics of expenditures for servicing and repayment of public debt in Ukraine in 2000-2015
Source: Calculated according to the Ministry of Finance of Ukraine.

To reduce the debt burden on the economy and the country's budget the foreign debt has been restructured. The IMF Programme on restructuring the foreign debt of Ukraine is aimed at meeting the following three objectives:

1 - savings in external debt payments of state debts and state-guaranteed debts, and public sector entities amounting to about 15.3 billion dollars for the period of the IMF Programme implementation;

2 - ensuring the ratio of public debt / GDP ratio of no higher than 71% by 2020;

3 - general support of the needs for budget funding on debt operations averaged 10% of GDP (up to 12% a year) in 2019-2025.

Restructuring external public debt was extremely necessary as far as it enabled the country to avoid default. According to the agreements signed with international lenders Ukraine was written off 3.8 billion dollars, and the terms for remaining debt amount payment – 15.5 billion dollars was respited for four years – from 2015-2023 to 2019-2027, but the rate of new Eurobonds yield increased to 7.75% per annum. For this purpose, instead of the existing 14 Eurobond issues (11 sovereign and 3 guaranteed by the state "Fininpro") and several state-guaranteed loans ("Ukravtodor", CB "Pivdenne" and "Ukrmedsnab") with an average coupon rate of 7.22% per annum 9 issues of roughly equal in volume new dollar Eurobonds repayable annually in 2019-2027 will be released, with the coupon rate of 7.75% per annum. The accrued interests on existing securities will be capitalized into new Eurobonds.

In addition, the holders of Eurobonds in proportion to their share in the total restructured debt will get 20-year state derivatives. Payments for them will be made in cash in dollars, depending on the dynamics of growth of real gross domestic product of Ukraine. If the GDP growth for the year is below 3%, the payment for the securities will fail. If real GDP growth is between 3% and 4% the payment for the securities will amount to exceeding 15% of GDP over 3%, and if it is more than 4% it will account for plus 40% of exceeding GDP index over 4%.

These derivatives provided by the Government will act only after the nominal GDP of Ukraine increases 1.5 times and reaches $ 125.4 billion (current IMF forecast in terms of GDP for 2019 in US dollars, which is equivalent to 3.183 trillion UAH under the current exchange rate). In 2021-2025 the state payments for derivatives (VRI) will be limited to 1% of GDP.

The restructuring and write-offs of a part of public debt enables to reduce debt risks and mitigate the debt burden on the economy. Successful debt restructuring, ensuring its stability, stabilizing the exchange rate, and real reforming of the banking sector and energy sector are key principles for positive decisions of rating agencies on long-term sovereign credit rating of Ukraine. The credit rating improvement of Ukraine at the end of November 2015 by the rating agencies of Fitch and Moody's from the level of "limited default probability " to the level of CCC and from Ca level to Caa3 respectively, is an important step to return Ukraine to the international capital market in the medium term, as stipulated by the IMF expanded funding program.

The growth of Ukraine's credit rating also facilitates Ukrainian companies and banks' access to international credit resources, and enables them to optimize their work in domestic and international markets. This will facilitate gradual recovery of the country's position in the international capital market and its macro-financial and macroeconomic stabilization. According to the World Bank forecast, under moderate economic recovery, gradual stabilization of the exchange rate and support of fiscal discipline, the public debt and the state guaranteed debt will be reduced by 2017 to 82% of GDP. Reducing the negative impact of the high levelled public debt on economic processes is actually possible under the condition of structural reforms in the economy, sustainable economic development, and comprehensive reforms in the fiscal area.

The public debt is correlated with the monetary and credit policy tools. The rising public debt is one of the reasons for rapid increase in money supply and inflation exacerbation. The modern financial studies include research mainly arguing interdependence of public debt and inflation. In particular, American economists T. Sargent and N. Wallace in the article "Some Unpleasant Monetarist Arithmetic" hypothesize that in the long run the debt service will lead to higher inflation rates than the deficit financing by the Central Bank's issuing loans. That is inflation, as they stress; it is rather a fiscal than monetary phenomenon, as Nobel laureate Professor M. Friedman argued (Sargent T., Wallace N.:1981, p.45.)

This is confirmed by a number of empirical studies. Specifically, American scientists L.Katayo and M. Terrones have analyzed statistics of the countries with emerging markets, developing countries and these with transition economies for 1970-2001. They revealed a strong direct relationship between the fiscal deficit and inflation (Catao L., Terrones M.: 2003, p. 14). Insufficient tax incomes, political instability, and limited access to external loans are observed in these countries.

However, some scientists deny the relationship between the deficit, debt and inflation. In particular, V. Biuiter argues that the growth of public debt does not lead to a proportional increase in inflation rate, but is partly compensated by a decrease in the market value of debt (Buiter W.H.:1999, p.p. 34-35).

Despite the controversies in explaining the dynamics of inflation – its monetary or non-monetary origin – modern theoretical approaches to the analysis of the relationship between fiscal and monetary-credit policy allowed to form a rather coherent direction of economic science concerning the fiscal discipline as a prerequisite for monetary stability. Today, it is generally accepted that preventing excessive spending on the public debt servicing requires institutional coordination between the Central Bank and the Ministry of Finance on the volume of its monetization.

Our studies show that between the monetary aggregates and public debt there are immediate and direct inverse correlations (Fig. 2). Based on our analysis of the relationship between the monetary aggregates and public debt in the 2000-2016 in Ukraine the conclusion was made that the greatest impact on the financial situation is produced by monetary aggregates M0 and M1. At that, the growth of debt by 1% causes a 9% increase in the monetary base and nearly 1% in cash and transferable deposits. And conversely, the impact of less liquid assets is much weaker compared to the aggregate of M0 and M1.

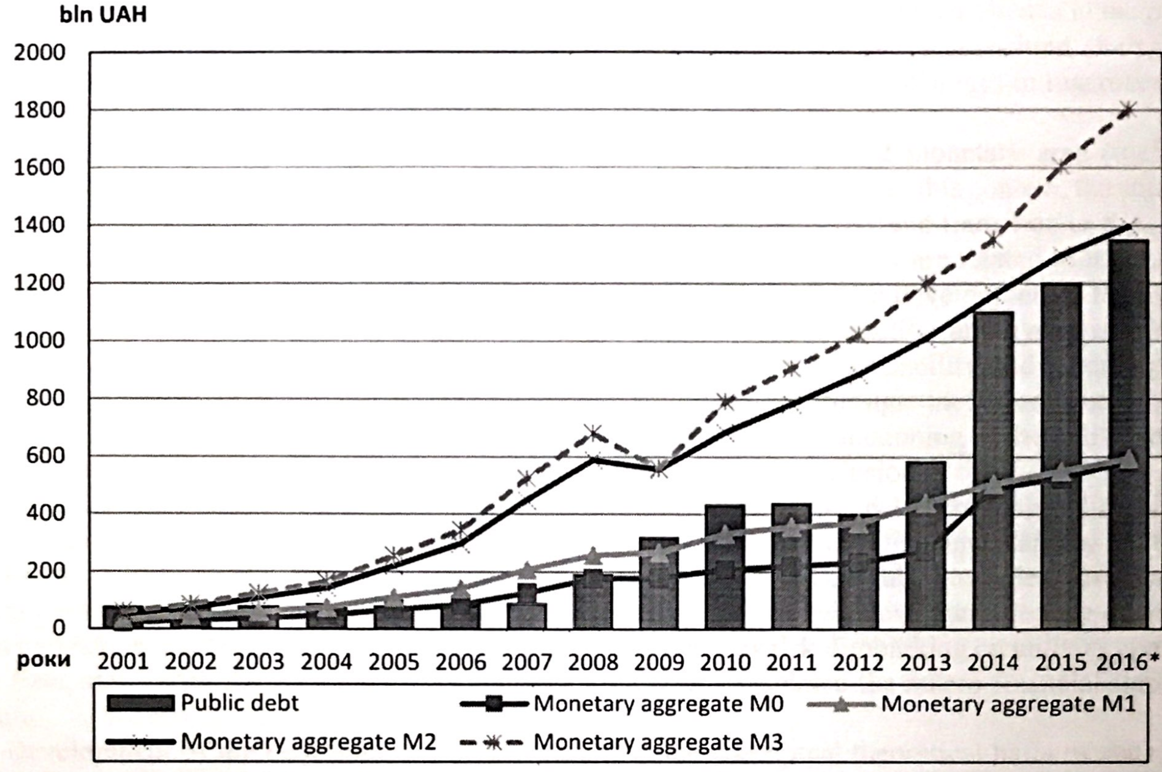

Fig. 2. Relationship of Monetary Aggregates and the Volume of Public Debt in Ukraine in 2000-2015
Source: Calculated on the basis of the National Bank of Ukraine.

Budget deficits and rising public debt lead to higher prices for financial resources, and, conversely, reduction of the deficit and / or achievement of budget surplus and reduction of public debt results in lower prices. In Ukraine, the growth of public debt almost by 2 times in 2008 (from 12.7% of GDP in 2007 to 20% of GDP in 2008) has been a factor for increasing of both, almost half the yield of government bonds and lending rates. Thus, the average weighted yield of government bonds with 6.71% in 2007 increased to 11.86% in 2008, the NBU discount rate, respectively – from 8% to 12%, the weighted average rate on loans – from 13.9% to 17.6%. In 2013-2015, because of the rising debt and the increase in the cost of government borrowing up to 18-23% per annum, the real rate on loans rose up to 25-35%, which minimized the credit activity. Thus, accumulation of public debt has been accompanied by the rising cost of government borrowing, causing increased prices on financial resources, increased rates on loans, reorientation of banks at the government lending. As a result, the monetary stability has been disrupted and threats to macroeconomic and macro-financial balance in the country have been created.

The public debt as a result of the system of government credit produces positive and negative economic, fiscal and social effects. Due to the government loans, the tax burden in certain periods could be actually reduced, compensating its fiscal consequences through higher taxes in future periods. This enables to have a certain economic, fiscal and social effects, having created conditions for meeting the needs of the fisk in the future. Negative effects of public borrowing are due to their form of tax anticipation, and that leads to further escalation of the crisis of government finance. The burden of public debt directly leads to additional taxation, which is necessary to paying and servicing the public debt. This process, in its turn, increases driving out private investment.

In summary, the magnitude of the effects of public debt directly depends on the nature of the loans and the value of reducing national savings (private and public). The recent authors' calculations and causation analysis of the negative effects of the public debt growth allow us to conclude that the debt increase in Ukraine in 2008-2015 led to a decrease in investment, sharp decline in industrial production and exports, decline in well-being of the population, and that rather worsened the macroeconomic and macro-financial situation, and became one of the factors for pre-default state of the country. Based on the calculations it was established through the tools of economic-mathematical modelling that the growth of public debt by 1% leads to an increase of the tax rate by 0.1%, budget expenditures – by 0.03%, the budget deficit – by 0.36%, the index of consumer prices – by 5.58%, the yield of government bonds in the primary market – by 0.15%, reduction of capital investment – by 2%, and reduction in household savings – by 1.88%. And conversely, the reduction of public debt usually leads to positive changes in macroeconomic indicators.

The economic and social effects are reflected both in the fiscal and monetary area (ineffective National Bank's rate policy in Ukraine on maintaining the national currency). In this context, the state faces important and difficult tasks because of the changes in exchange rate policy and transition to the floating exchange rate, and further transition to the regime of inflation targeting. They are related to the necessity of macroeconomic and macro-financial stability, structural reforms and further development of the financial market. Economic, fiscal and social effects are aggravated through interaction and synergistic effects, manifested in negative consequences and side effects for macro-financial stability and macroeconomic balance. This results in the effect of private investment crowding through inefficient use of public borrowings, directing them for the current consumption, and inefficient functioning of the public sector as a whole. Ukrainian realities clearly demonstrate the validity of these conclusions.

Thus, the debt policy in Ukraine requires radical reformation. Irrational borrowing policy aimed at meeting the current needs of the Government has exacerbated risks to macro-financial stability in Ukraine. In 2014-2015, like in 1998-1999, the country was on the brink of the default. Inefficient fiscal and tax policies, lack of structural reforms in the energy sector and dollarized debt have increased the quasi-fiscal deficit component, and increased the debt vulnerability to a currency risk. Embarking on military operations in the East, along with the accumulated imbalances, significantly violated the macro-financial stability of the state.

Development of the debt policy should be based on the conceptual theoretical basis of state credit, through thorough understanding of the essence and nature of this complex, multifaceted and multispectral category. The debt policy should be aimed at implementing the public purpose of government credit, that is, to contribute to maximal financial opportunities of the fisk in order to provide financial resources necessary for the public welfare and sustainable economic growth. It really should be an integral part of fiscal policy and a single system of macroeconomic and macro-financial regulation.

Conclusions

The debt policy should include both strategies and tactics. The debt strategies should specify goals, objectives and methods of their achieving in the long term. The strategy should define the threshold and optimal size of debt, the debt structure, loan tools with the restrictions of value, terms and specification of currency, and trends. The strategy should also evaluate effectiveness of the use of the borrowed funds. The debt strategy should be based on a new generation of fiscal rules that limit the size of debt and deficit, depending on the stage of the economic cycle, providing the effect of automatic stabilizers and allowing some flexibility in application of countercyclical fiscal policy to counter significant downturns in the economy.

The debt strategy should be approved at the legislative level, which will reduce the possibility of executive power to change the volume and structure of the borrowings depending on operational requirements for covering budget expenditures, and will ensure precise performance of the tasks for current and next governments in future periods. In order to achieve short-term goals it is necessary to clearly outline the objectives of the debt tactics, the mechanism of its implementation, the forms, methods and tools to be adapted to the needs of fiscal policy. The debt tactic tasks should be developed in the context of implementation of debt strategy objectives, consistent with the task of fiscal and monetary, and credit policy in the short term.

The development and implementation of the effective fiscal, debt, monetary and credit policy requires precise action coordination, especially that of the Ministry of Finance of Ukraine and the National Bank of Ukraine. That coordination should be made by the special Council (Commission) consisting of the representatives of interested Ministries and Agencies under the Cabinet of Ministers of Ukraine. In this regard, it is proposed that the Cabinet of Ministers of Ukraine develop and approve the only document, i.e. "Principles of Fiscal, Debt, and Monetary and Credit Policy," where all provisions should be mutually agreed and coordinated regarding actions and time dimensions. The coordination should include all phases of development and implementation of fiscal, debt, and monetary and credit policy along with improvement of financial market infrastructure, development of the secondary market for government securities, information provision, and mainly – clarity and transparency in the actions of all concerned institutions on the financial market.

The adoption of the "Strategic Plan of the Ministry of Finance of Ukraine for 2015 budget year and two budget periods following the planned (2016-2017)" and "Basic Principles of Monetary Policy for 2016-2020 " should be positively assessed, as far as these documents determine fiscal priorities and monetary policy for 2017 and 2020 respectively. However, the coordination of actions should be improved on the use of government securities as fiscal and monetary tools that respectively will increase the efficiency of public debt management. The effective coordination of fiscal, debt, and monetary and credit policy in Ukraine needs clear and transparent European fiscal and monetary rules on which fiscal, debt and monetary and credit strategy should be based. A comprehensive approach to the definition of fiscal, debt, and monetary and credit policy, should be based on the principle of tools and mechanisms complementarity and take into account the EU practices. Only this approach will ensure the effectiveness of macro-financial adjustment to provide a sustainable economic development.

For Ukraine, the optimal ratio of public debt to GDP should be lower than that for advanced economies because of high risks, a significant proportion of foreign currency debt, lower efficiency of the public sector, and insufficient development of the financial market and institutional environment. We propose to legislate the maximum size of the public debt of Ukraine, under normal economic conditions, of 35% - 40% of GDP. The debt strategy should define the optimal structure of government borrowings. Gradually the debt policy of Ukraine should be focused on foreign debt reduction that now prevails in the structure of public debt, and also on the increase of borrowing on the domestic market. Fundamentally, attracting foreign loans is not conducive to the development of the full-fledged domestic financial market, because under low institutional environment, foreign resources are not always used with maximum efficiency. Moreover, if in the short run, the debt servicing costs are reduced (because of lower interest rates on foreign loans compared to internal), in the long run, these positive effects offset because of the increased economic vulnerability. A large proportion of external debt in the debt structure results in high risks for fiscal stability.

This leads to a considerable vulnerability of national financial system, to external shocks, and dependence on the behaviour of foreign investors. According to the IMF experts, in the countries with emerging markets, the critical share of debt denominated in foreign currencies in the total amount of public debt makes 40.3% (although the median for the countries with emerging markets in the period of 1995-2010 was 56%). Accordingly, the minimum permissible value of the debt share denominated in local currency is 59,7% (Yaroshenko F.O.:2015).

Simulation modelling of currency structure of the government debt portfolio in Ukraine, conducted by Ukrainian financiers A. Fedosov and O. Kolot in 2008, produced the following results: reduction of the sensitivity of debt payments in each of the borrowed currencies to fluctuations of relative exchange rates requires a corresponding increase in the share of commitments in hryvnia up to 53% (Fedosov V., Kolot A.A.: 2008, p.30). Thus, the results of the research indicate that the proportion of domestic currency debt in total public and publicly guaranteed debt of Ukraine may account for 50% - 55%.

Today, the increase of the domestic borrowing share in Ukraine should be done by attracting institutional investors. The banking system resources under the recession should be directed primarily to real economy lending, against the Government's needs. It is just the institutional investors, accumulating small depositors and individuals' funds, who are among the main buyers of government bonds in many countries. The urgent task is to attract passive investors to the market of loans in connection with the development of storage mechanisms for social problems' solution in the area of government finance, in particular, pension provision. The choice of borrowing tools should be grounded by the choice of government credit forms, the use of which will maximally meet the objectives of debt policy. Today, Ukraine should diversify the tools of government borrowings, in particular, to issue various types of bonds, like savings bonds, retail bonds, bonds denominated in several currencies thus attracting different groups of investors to the market.

Particular weight in the reform of the debt policy is to determine the directions for application of the state borrowed funds. It should be noted, that in Ukraine the efficient use of the debt finance potential is weak. The bulk of borrowed funds by means of loans is used to finance the current budget expenditures. In case of necessary macroeconomic and macro-financial stability, and sustainable development, the attracted funds through loans should be used for specific investment projects, and their use be minimized for financing the current budget spending. Therefore, using the mechanisms and tools of debt policy raises the risks of loan financing for macro-financial stability when it is not substantiated by theoretical studies. Specifically, the debt policy, based on modern concepts of public credit operation, will enable to identify the advantages and disadvantages of debt financing of budget expenditures, to reveal the potential of debt finance, which will transform the public debt from the burden into an asset of the nation.

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