**Case Study (Intro to International Business)**

***Assignment Regulation:***

* Citing of references is necessary.

***Learning Outcomes:***

* Identify the major components of international business management (Lo 1.2)
* Explain the forces driving and evaluate the impact of globalization (Lo 1.3)
* Discuss the reasons for and methods of governments’ intervention in trade (Lo 1.7)
* Identify and evaluate the significant trade agreements affecting global commerce (Lo 1.8)
* Carry out effective self-evaluation through discussing economic systems in the international business context (Lo. 3.6)

**The IMF and Ukraine’s Economic Crisis**

Back in late 2013, the then-president of Ukraine, Viktor Yanukovych, suspended preparations for the implementation of a trade agreement with the European Union, opting instead for closer ties with Russia. Yanukovych’s decision resulted in mass protests in the capital city Kiev and elsewhere in western Ukraine, where closer ties with the West were seen as a necessary counterbalance to the growing influence of its powerful neighbor to the east, the increasingly autocratic Russia of Vladimir Putin. These protests ultimately led to Yanukovych’s ouster from office in February 2014. Following his removal, unrest enveloped the largely Russian-speaking provinces of eastern and southern Ukraine from which he had drawn his support. In March 2014, the autonomous region of Crimea was annexed by Russia, while a civil war between the new Ukrainian government and pro-Russian separatists developed in eastern Ukraine.

The result was an economic disaster for Ukraine. In 2014, the country’s GDP shrank by nearly 10 percent. The currency, the hryvina, fell by more than 50 percent against other currencies as capital fled the country. As the costs of imports rose, inflation jumped from 1 to 25 percent. In a desperate attempt to support the value of its currency, Ukraine’s central bank bought hryvina on the foreign exchange market, selling its foreign currency reserves to do so. Ukraine’s foreign exchange reserves declined from more than $16 billion in mid-2014 to under $6 billion by early 2015. Moreover, the country was facing debt repayments of at least $10 billion and gas import bills from Russia, while its own banking system was shattered. In an attempt to pull Ukraine out of an economic tailspin, in April 2014, the International Monetary Fund (IMF) pledged to contribute $17 billion in loans to the country over two years, of which about $5 billion was disbursed in 2014. It wasn’t enough. The currency continued to lose value, inflation increased, unemployment rose, and the economy shrank. In early March 2015, the IMF deepened its involvement in the country, putting together a package of additional financial support. The IMF agreed to a four-year deal to loan $17.5 billion to Ukraine. The deal was expected to unlock another $20 billion in loans from the United States and the European Union.

In return for these funds, which were to be used to support the value of the hryvina in foreign exchange markets, Ukraine had to agree to a raft of policies imposed at the bequest of the IMF. The country agreed to maintain a

free floating exchange rate and to pursue a tight monetary policy aimed at restoring price stability. The state-owned natural gas company, Naftogaz, was also required to increase its prices by as much as 200 percent. Naftogaz had been buying natural gas at market prices from Russia and selling it at deeply subsidized prices to Ukrainians. This money-losing transaction had been financed by issuing debt, which the government could no longer service. Indeed, a growing debt burden and excessive government spending were major problems facing the country. These problems only got worse as both the economy and the tax base contracted. At the insistence of the IMF, the Ukrainian government also agreed to cut spending on unemployment and disability insurance, to reduce the salaries of state workers, and to cut state pensions.

The IMF believed that while these austerity policies would result in the economy shrinking by a further 5 percent in 2015, the economy would start growing again in 2016. Unfortunately, conditions in Ukraine deteriorated further in 2015. After some initial success, the Ukrainian government pulled back from implementing the full raft

of austerity policies proposed by the IMF. To make matters worse, there was evidence that some of the IMF loans were being syphoned off or squandered by corrupt government officials. In October 2015, the IMF responded by halting its dispersal of funds under the loan program and pressuring Ukraine to institute economic reforms and tackle government corruption. With funds from the IMF on hold, the Ukrainian economy continued to decline, shrinking by an estimated 11 percent in 2015. Unemployment continued to rise, and the inflation rate jumped to around 50 percent.

In February 2016, Christine Lagarde, the managing director of the IMF, stated, “Without a substantial new effort to invigorate governance reforms and fight corruption, it is hard to see how the IMF supported program can continue to be successful.” Lagarde’s comments followed the resignation of Ukraine’s economic minister after he accused a senior aide to the president of blocking anticorruption reforms. Following Lagarde’s comments, the Ukrainian government pledged to step up its efforts to fight political corruption and introduce economic reforms but cautioned that changes could not be made overnight. In April 2017, the IMF unlocked another $1 billion of support for the Ukraine after the government had taken IMF-mandated steps to rein in the budget, crack down on corruption, and improve the investment climate. However, the IMF stressed that further structural reforms are necessary to achieve faster economic growth, including reforming government pensions, tougher corruption measures, and privatizations.

**Case Discussion Questions**

1. Why do you think Viktor Yanukovych walked away from a trade agreement with the EU in favor of closer ties with Russia? What did he gain by doing this? What did he lose?
2. What were the root causes of Ukraine’s currency crisis? Without help from the IMF, what might have happened?
3. Were the policy recommendations made by the IMF reasonable?
4. Why do you think the Ukrainian government balked at fully implementing the IMF policies?
5. Was the IMF right to suspend disbursement of monies under its loan program in October 2015? Under what conditions should the IMF resume making loans?
6. What might happen if the IMF discontinues its loan program to Ukraine, as it has threatened to do?
7. Could the IMF have done anything differently to avoid the situation it now finds itself in?

Please mention the references.