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# Government loan in the conditions of Ukraine's new challenges

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## *Abstract*

The article substantiates the need for public lending to cover the state budget deficit at the present stage, examines the current state of Ukraine's public debt and analyzes main indicators of Ukraine's debt security.

**Key words:** credit, military bonds, budget, expenditures, grant.

## *Introduction*

The state, as a subject of economic relations, uses not only budget revenues, but also additional financial resources, formed on a loan basis, to finance its expenditures. The way to involve them in budget expenditures is public credit. It represents a specific part of the sphere of public finance, as it does not have separate financial funds, as the funds mobilized with its help, usually go through the budget. However, it characterizes a special form of financial relations between the state and other participants in credit relations, and therefore stands out in a separate link.

Most countries now have budget deficits and use credit to repay them. Public credit is becoming an increasingly popular way to finance the budget. This can be said by seeing the dynamics of global public debt, which is growing steadily. For Ukraine, the role of public credit is becoming increasingly important as new threats and challenges emerge that require additional sources of budget funding. The role of public credit became especially important in 2020-2022, when due to the epidemic, and later – military aggression, there was a significant budget deficit, which required significant borrowing to finance.

**Analysis of recent research and publications.** Well-known domestic scientists – I. O. February, V. A. Andrushchenko, O. P. Bliznyuk, O. V. Plotnikov, I. Y. Chugunov, Y. V. Onishchuk, P. S. Yeshchenko, I. O. Lunina and others.

## *Results and Discussion*

After the start of a full-scale war of the Armed Forces of the Russian Federation against Ukraine on February 24, 2022, in March of the same year, the Ministry of Finance began auctions for the sale of military bonds.

Military bonds are a type of domestic government bonds or government securities issued by the Ministry of Finance of Ukraine. Military bonds are placed by the government on the domestic government securities market in Ukraine. Their peculiarity is that military bonds are targeted. This means that the state will use the funds from their placement to finance the Armed Forces of Ukraine, as well as the needs of our country in martial law.

The state will guarantee the owners of military bonds the payment of their nominal value and income from them, in accordance with the announced conditions of placement of bonds.

Military bonds are a powerful investment tool to support the state budget, available to citizens, businesses and foreign investors in times of military threat.

Funds from the sale of bonds, attracted to the State Budget of Ukraine, are used for uninterrupted and constant provision of social and defense financial needs of our state in martial law.

Military bonds are securities issued by the government to finance military expenditures. This is not an invention of the Ukrainian Ministry of Finance. This tool was used by other countries, especially in the XX century. For example, the United States issued Freedom bonds to participate in World War I and to support the Allies. Other participants in that war did the same.

In the case of Ukrainian military bonds, it is not just about financing the army. The money from their placement is attracted to the state budget, where the government can spend it on any wartime needs, not just the defense industry.

The nominal value of one bond is UAH 1,000, and the value of foreign currency bonds is UAH 1,000 or EUR, respectively. Initially, securities from the Ministry of Finance are bought by primary dealers and licensed brokers (banks, investment funds, other financial institutions), who then sell them on the secondary market to their clients.

There are short-term, medium-term and long-term bonds with a maturity of 2 to 15 months. The rate of return on these securities is 9.5 – 11% per annum. The placement of long-term bonds involves interim interest payments (How to buy Ivy bonds).

Also, the Ministry of Finance issues bonds in US dollars and euros, the yield on foreign currency military bonds – 3.7% and 2.5% per annum, respectively.

According to the National Bank, on April 27, the owners of securities (about 1,000 legal entities and individuals) received UAH 3.3 billion from the redemption of the first bond issue. Some of them were re-invested by investors in domestic government bonds (NBU).

Military bonds have the same advantages as “peaceful” IGLBs – no taxes or fees are required on such income, unlike, for example, bank deposits.

Military bonds are guaranteed by the state. That is, the state is the debtor and guarantees the return of invested funds together with interest income. The government has greatly simplified the procedure for purchasing such securities during the war. In particular, it is not necessary to confirm the source of the invested funds.

At the same time, it is necessary to pay attention to the following rule: if the amount exceeds UAH 400,000, the bank “is obliged to inform the client about the need to establish the sources of credited funds in case of client expenditures” (How and where to buy military bonds).

That is, to get the money back, you still have to prove the sources of their origin. The banks with which the Ministry of Finance communicated also confirmed the need to prepare relevant documents (How and where to buy military bonds).

Given that the National Bank of Ukraine forecasts about 20% inflation by the end of 2022, the purchase of military bonds will help at least partially offset it.

Any investor, including a non-resident, can buy military bonds. Terms of purchase of military bonds may differ in different banks and financial institutions. First of all, you need to pay attention to the minimum amount of your investment. For example, in Raiffeisen Bank and OTP Bank the sale starts from UAH 500,000. (500 bonds), in Taskombank – from 300,000. In PrivatBank you can buy from 100 bonds (i.e. minimum entry – UAH 100,000), in Sberbank – from 50 (UAH 50,000).

However, many banks and organizations are willing to sell on a single bond, which is convenient for small investors. The easiest way to buy is a mobile application. Such a service is offered, in particular, by Ukrgasbank, FUIB, Monobank, ICU brokers, Univer Capital, BTS Broker. The Minister of Digital Information announced that in June 2022 it will be possible to purchase these papers in the mobile application “Action” (Military bonds).

When buying these securities, it is important to study the terms of their sale and maintenance, including the amount of fees charged. At the same time, most sellers do not charge a commission.

As of May 2, according to the NBU, 11,800 citizens and business representatives have invested in military IGLBs, their total portfolio is UAH 3.5 billion \$ 38.3 million and 25.4 million euros. Non-residents have over UAH 66 million (NBU).

The main conditions for buying and selling military bonds include:

- ✓ the service is provided to individuals – residents of Ukraine;
- ✓ possible currency of military bonds – hryvnia, US dollars, euros;
- ✓ maximum amount of military bond purchases per day – depends on the bank or broker;
- ✓ personal income tax and military duty is not withheld;
- ✓ personal income tax and military duty is not withheld;
- ✓ according to the decision of the NBU when buying military bonds check sources;
- ✓ origin of funds is not carried out;
- ✓ income on military bonds can be obtained in the form of:
  - interest income – on interest-bearing bonds;
  - the difference between the purchase price and the nominal value of securities that arises when redemption of military bonds;
- ✓ redemption of military bonds and payment of income is made in the currency of bonds on time;
- ✓ established by the terms of the bond issue;
- ✓ the results of the placement of military bonds can be found on the website of the Ministry of Finance of Ukraine section “Public debt” → “IGLBs” → “Auction results”.

Every Tuesday, the Ministry of Finance holds auctions to sell military IGLBs. To date, the following tools are available (Table 1).

**Table 1 – Types of military bonds in circulation**

ISIN code military bonds	Maturity	Repayment date	Last post date	Rate
UAH				
UA4000225866	3 months	27.07.2022	24.05.2022	9,5%
UA4000225791	6 months	02.11.2022	24.05.2022	10%
UA4000225668	1 year	01.03.2023	22.03.2022	11%
UA4000225809	1 year	21.06.2023	03.05.2022	11%
UA4000225908	1.5 years	25.10.2023	24.05.2022	11,5%
U.S. dollar				
UA4000225775	1 year	27.04.2023	19.04.2022	3,7%
UA4000225874	1 year	25.05.2023	24.05.2022	3,7%
Euro				
UA4000222509	8 months	01.12.2022	24.05.2022	2,5%

Source: (Last week, almost 9,000 citizens).

Unlike other buyers, the National Bank does not participate in auctions, but buys military bonds on fixed terms: UAH 1,000. for bonds, their yield – 11%, maturity – 15 years. The relevant resolution of the Cabinet of Ministers states that the NBU can buy up to UAH 400 billion of such securities.

In fact, such a step is a covert issue and the activation of the “printing house”, which in which in peacetime the independent NBU almost does not use.

I would not go under any circumstances. The issue or printing of money leads to an increase in the money supply, while the number of goods and services does not grow at such a rate (and in conditions of war may decrease), which stimulates inflation. That is, money in the economy becomes more, they become cheaper, and their purchasing power decreases.

To curb rising prices, the National Bank imposed a number of restrictions, including on the movement of capital, and fixed the hryvnia exchange rate. At the same time, the National Bank spends its foreign exchange reserves in support of the national currency: at the beginning of May they decreased by \$ 1.5 billion to \$ 26.6 billion (How and where to buy military bonds).

The National Bank understands the inflationary risks of the “printing press”, so they emphasize that such a tool is used only to finance “critical budget expenditures in limited amounts”. Financing from the NBU cannot be the main source of covering state budget expenditures, said the head of the regulator Kyrylo Shevchenko.

In March-April, the National Bank repurchased military bonds worth UAH 70 billion. The regulator explained that this amount had to be published due to reduced own tax revenues and lack of international aid.

“The expediency of further operations to finance critical government expenditures through the purchase of IGLBs will continue to be determined by separate decisions of the National Bank”, the NBU press service said.

As of the end of May 2022, the volume of investments of Ukrainian citizens and businesses in military bonds is:

- UAH 7.8 billion. (10% of the total amount of purchased military IGLBs denominated in hryvnia);
- \$ 57.4 million The United States (29% of the total military IGLBs denominated in US dollars);
- EUR 26.6 million (11.7% of the total amount of IGLBs nominated in euro).

Non-residents own 300.4 military bonds UAH million (Last week, almost 9,000 citizens).

Since the beginning of the full-scale Russian invasion, the Ministry of Finance of Ukraine has already held 38 auctions for the sale of military bonds and has attracted to the state budget:

- UAH 77 billion;
- \$ 199 million USA;
- 229 million euros.

This is evidenced by the data of the depository of the National Bank of Ukraine (Last week, almost 9,000 citizens).

In hryvnia equivalent, funds raised from military bonds amounted to UAH 92 billion. This is:

- 5.7% of the planned annual revenues of the state budget in 2022 year;
- 67% of defense expenditures in January-April this year;
- 62.4% of the state budget deficit for January-April this year.

Such receipts to the state budget in modern conditions are extreme important because tax revenues cover only a third of expenditures. The other two thirds are loans and international financial assistance.

In the military situation, budget expenditures also increased. Currently, three quarters of the funds are spent on military needs, with UAH 10 billion to UAH 15 billion / month spent on humanitarian programs, including support for temporarily displaced persons and payments of UAH 6,500 / assistance (How to buy Ivy bonds).

“The budget is in such a state that we now look at our revenues in a secondary context, the primary one is how to attract international grant and credit assistance. Our revenues, according to the most optimistic estimates, now cover only one third of our expenditures. grant funds – internal and external”, – said Marchenko (NBU).

The largest portfolio of military bonds is concentrated in banks – primary dealers. At the same time, the demand of the population and business of Ukraine for relevant securities continues to grow. In particular, during the last week of spring the number of depositors among them increased from 67 thousand to almost 76 thousand people.

### **Conclusions**

The existing problems of the public credit management mechanism in Ukraine should be noted: weak development of the domestic stock market, which makes it difficult to attract government loans; rapid growth of government borrowing, which leads to a sharp increase in public debt; the tendency to increase the maturity of government securities in the loan market; the growing dynamics of the yield on domestic government bonds (IGLBs), which in turn contributes to increasing the cost of servicing government borrowing in the state budget.

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