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FAILURES OF THE UKRAINIAN ECONOMY AND USING THE EXPERIENCE OF THE EUROPEAN INTEGRATION OF NEIGHBOURING COUNTRIES TO OVERCOME THEM

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Abstract. *Introduction.* The most important task of every state is ensuring of citizens' welfare continuous growth. For centuries, the most famous economists of the world devoted their researches to this issue; they have substantiated the theoretical aspects and have given the practical recommendations for the effective management of national economies. However, using these recommendations, one should be aware that during the last two centuries in the organization and operation of complex economic systems, which are national economies, the significant changes associated with globalization and monopolization of markets, and strengthening the role of the state took place. *Purpose of the study.* In the article, the reasons that led to the deepening of the gap between Ukraine and mature economies over the last twenty-five years are researched, and it was proposed to use the experience of the European integration of neighbouring countries to overcome them. *Results.* It is substantiated that the cause of periodic recession of the Ukrainian economy in the nineties of the XX and early XXI century is neglecting of changes that have occurred in the laws of complex economic systems development in the XX century, the loss of state control over social and economic processes in the country, insufficient financing of scientific researches, and implementation of new technologies. It is shown the discrepancy in actions of the National Bank of Ukraine, the Ukrainian government and demands of the national economy for loans. *Conclusion.* In order to eliminate these causes and providing dynamic development of Ukraine, it is suggested to use the experience of the European integration of neighbouring countries, to create a favourable legal and tax climate to attract foreign and domestic investment, strengthen law enforcement activities for the unshadowing of the national economy, provide structural transformation of cost-inefficient and unprofitable industries, improve the system of taxation entities and persons incomes, ensure equitable distribution of incomes in the country. It is recommended to increase spending on state funding for science and innovation, and implement a set of measures in order to make loans available to local manufacturers and consumers.

Key words: Ukrainian economy, recession, European integration, tax burden, innovation, credit resources.

JEL Classification: E12, E52, O32

1. Introduction

The most important task of each state is to ensure the continued growth of the well-being of its citizens. Therefore, for many centuries, the most well-known economists of the world devoted their research to this issue, which substantiated the theoretical aspects and provided practical recommendations for the effective management of the economies of the countries, minimization of the consequences of possible crises, overcoming the recession and restoring economic growth. However, today, when using these recommendations, it must be taken into account that during the past two centuries, the organization and operation of complex economic systems, which are the economies of the countries, have undergone significant changes associated with globalization and monopolization of markets, as well as the strengthening of the role of the state. However, as evidenced the consequences of the management of the national economy of Ukraine over the past two and a half decades, the inconsistency of the actions of domestic government to the recommendations of scientists who have positively proven themselves in other countries, caused a long-term crisis. Thus, the purpose of the article is to reveal the reasons for the failures of the Ukrainian economy during the period of independence and to substantiate the recommendations for ensuring its dynamic development.

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2. Lagging of Ukraine in economic development from neighbouring countries

Ukraine which has significant scientific, economic, natural, and employment potential, remained behind the European economy over the past twenty-six years. In 1990 Ukraine left behind its western neighbours Bulgaria and Romania according to the production of the gross domestic product (GDP) per capita respectively by 7.6 and 4.4% and was inferior to Poland by 0.9%. In 2016, it was already behind them respectively by 1.23, 1.45 and 1.51 times (State Statistics Service Ukraine, 2016).

At the same time during the past twenty-six years, the lag of Ukraine according to the economic indexes increased from the Baltic countries which were a part of the Soviet Union until the nineties of the twentieth century. In 1990, the production of GDP per capita in Lithuania, Latvia, and Estonia left behind Ukraine respectively by 49.5, 51.4 and 18.8% and in 2016 the gap increased to 1.6–1.8 times.

The abovementioned information proves the correctness of the European integration path chosen by the following countries: western (Poland, Bulgaria, Romania, etc.) and northwest (Latvia, Lithuania, and Estonia) neighbours of Ukraine, and global mistakes prevented by the Ukrainian government in determining and implementing the strategic direction of its development.

3. Causes of failure of the Ukrainian economy

In 2014, Ukraine ratified the agreement on the Association with the European Union with the aim to expand the target market for its products and to get rid of all economic problems. However, the country does very little those who create the wealth of the country could have good conditions for free entrepreneurship, reliable and equitable contractual protection, and have the deserving conditions for work and rest.

So, it is necessary to analyse the reasons that led to the failure of the national economy in the past two decades and to propose a conceptual approach to the formulation and implementation of the strategic directions of development of Ukraine in the future. Thus, our country's joining to the European values should be considered as a goal but not as means of overcoming the results of the mistakes that caused a long-term recession.

Eastern Europe countries after refusing the command and administrative methods of management followed the way of creating a favourable environment for national companies business and attracting foreign investors for the successful development of their economies. To do this, they had to do a lot of work: rapid privatization of state assets, including its returning to "old" owners; liberalization of relations between state institutions and commercial firms; the adoption of clear, stable, and with optimal load tax laws, and laws that ensure the minimization of corruption schemes.

Ukraine had another situation after it had got the independence. In the early nineties, in the conditions of the economic downturn, the native legislators and officials had the only way to increase the revenue to the state budget and output of the economy from the crisis. It was the increasing of the tax load on the taxpayers. In some years (1994–1996), the tax load on business in our country reached 50% or was higher than the same indexes in other countries during the stable periods of their economies by 2–3 times. The wage bill had especially high load – more than 40%.

Thus, Ukraine, determining the strategy of its development after having got the independence, did not take into consideration the experience of other countries, which for various reasons faced complex economic problems that prompted them to seek optimal ways of development.

The situation that took place in Ukraine at the end of the last century was typical for economically developed countries during the Great Depression in the 20–30 years of the twentieth century, and for Western Europe and Japan in the post-war period. At that time, the tax load on businesses in those countries was much lower. Thus, in 1937 the ratio of tax revenues of the economically developed countries of Europe to the national GDP averaged 16.5%, and in some countries much less: Switzerland – 6.0, Sweden – 8.5, Norway – 10.9%.

In 1965, the tax load on businesses in the world increased significantly: the average tax load in the industrialized countries of Europe was 28.6%, and of other continents – 23.2%. However, in that year in Japan, which had just renewed its economy, this index was 18.3%, and in the United States that spend huge funds on the militarization of the country, this index was 25.0% (Amosha, Vyshnevskyy, 2002).

Thus, the legislators of the Western countries made it possible to "stand up" to domestic producers and only then by the way of gradually increasing the tax load provide a high level of social security.

Of course, Ukrainian legislators and government officials can be understood. During the break of the ties between the former republics of the Soviet Union and the collapse of the national economy, they had a difficult choice: on the one hand, it was necessary to reduce the tax load on manufacturers to promote their recovery, on the other hand, the social programmes and the need of the maintenance of the budgetary institutions required the increasing amounts of funds. Under these conditions, the native leaders considered relying on the idea of those classics of market economic theory who believed that the market was able to stabilize itself. Although in 1936, the world-famous economist John Maynard Keynes concluded that the state should pursue the stabilization policies in order to prevent the economic crisis or to avoid its developing (Keynes, 2007).

One of the key principles of a market economy that is built by Ukraine from the time of having got the independence is to create the conditions for the free initiative expression at all the levels of the economy. The talent, initiative, and dedication are the determinant factors that should ensure a decent level of income for each person if they are the quality of the individual, the company, and the region led by leaders with these qualities.

That is why in order to encourage initiative, dedication, and talent which are the basis of the dynamic growth of any country, it is necessary to create the conditions, under which everyone regardless of his/her status could realize their potential and fulfils their dreams. Adam Smith in his fundamental work "An Inquiry into the Nature and Causes of the Wealth of Nations" grounded that a man is driven by the inclination for self-enrichment. But every person who is guided by selfish motives and cares only about his/her interests actually helps everyone and thus increases the "wealth of nations" (Smith, 1962).

So, according to these political economy classic's conclusions, to ensure the dynamic development of the national economy, Ukraine had to create the conditions for displaying private initiative and free competition of producers and consumers, that is, to liberalize the economic relations in the country and to ensure their legal protection. Actually, this way was followed by Ukraine in the early nineties of the last century.

However, the cataclysmic decline in production of goods and services caused by rupture of long-term relationships, while increasing the tax load and the devaluation of the national currency, created a favourable environment for corruption and shadowing of a large part of the domestic economy, the destruction of one and enrich of the other part of the population. At the same time, uncertainty about the future and the thirst for profit made even the successful businessmen think about the present delaying the upgrades of companies in the future. This led to a loss of competitiveness of Ukrainian products and the displacement of it from Ukrainian and international markets by foreign competitors.

So, *first of the reasons* that caused the current failure of Ukrainian economy is the ignoring by the native leaders the changes that took place in the laws of economic systems within more than two hundred years after the first works of Adam Smith. Adam Smith pointed out those external influences, when they become powerful, can disrupt this wonderful market property (to self-control – Author).

It should be noted that many economists (the most prominent was John Maynard Keynes) grounded that the totally free competition cannot exist in nature (Keynes, 1999) as the market is constantly influenced by a lot of things: monopoly (natural or artificial), public administration (increased spending on social programmes and government spending), other countries (protectionist measures to protect their own producers), the uneven distribution of mineral resources and varying soil fertility, transport spending and others, that even through a comparative advantages in other sectors of the economy do not allow the country to balance its import and export and to provide the same cost of domestic product with other countries because of the monopoly of trade union actions, the capitalists' rush for excess profits, because of the corruption in public administration and regulation, and the shadowing of part of the economy that avoiding from taxes gets an advantage over its "honest" colleagues, because of the lack of true freedom for "economic" person (access to knowledge, jobs, credits, etc.), and war and political conflicts.

In fact, Ukraine had nearly all of the abovementioned problems in the early nineties of the twentieth century: the newly created monopolies began to dictate the price of imported oil, petroleum products, and natural gas. Ukraine could provide itself with this domestic production only by 15-20% that caused the adverse balance of foreign trade; the share of public expenditure on social protection and social security of the population increased; Russia began the program for the replacement of most products, which had been produced in Ukraine; mass social movements caused not always thought-out closing of environmentally dangerous enterprises; there were a lot of strikes caused by delay of salaries; new businessmen in the rush for excess profits stopped at nothing, even at illegal methods and infringement; corruption and the shadow economy acquired the unprecedented sizes; the credit resources became inaccessible to most enterprises due to the devaluation of the currency and financial instability; the level of higher education levelled and the best scientific personnel left the country; Ukraine suffered from the constant political pressure from its northern neighbour.

Under these conditions, Ukraine defining the strategies of its development had to take into account the changes that had occurred in the world economy in the twentieth century. For example, that the modern economies are much more export-import dependent on the external environment that leads to fast (in recent years lightning) transfer of economic crisis from one country to another (it was the most typical during the economic crisis of 1998).

That is why Ukraine, which, on the one hand, suffered from Russia's pressure and, on the other hand, was unable to penetrate with their products to Western markets along with the liberalization of economic relations in the country and creating a favourable business environment, had to strengthen the role of state institutions in order to concentrate the efforts of the whole society to update products and to prevent monopolization and the shadowing of the national economy, the corruption wide-spreading, and massive impoverishment of the population.

The *second reason*, which follows from the first one and which greatly extended the structural and economic crisis in Ukraine in the nineties of the twentieth century, is the loss of real control over economic processes in the country by state institutions.

Under such conditions, the following things happened: a rapid separation of income across the population, moving abroad of the most active part of Ukrainian society, rising of unemployment and loss of motivation for effective work for those who worked at domestic enterprises. However, the state expenditures were directed mainly not to the innovation of products, and to support the material and energy-intensive industries. At the same time, the costs of maintaining the growing number of ineffective public administration and members of law enforcement agencies.

As a result of this economic policy from 1990 to 1997, the percentage of newly formed engineering products in Ukraine, which conformed to the native and international analogues, decreased by 23.9 points from 88.9% to 65.0% while the rate of the products, which is lower than the existing analogues or is not defined, increased from 7.2% in 1990 to 33.3% in 1997 or by 4.6 times (State Statistics Service Ukraine, 2016).

That is why the lack of radical reforms, for example, the substantial decrease of the tax load on businesses and priority funding of the *high-tech industries* prevented the Ukrainian economy even during the five-year 6-10% GDP growth in 2000-2007 to provide product updating and significant improvement of the living standards. During this period, the GDP growth of Ukraine was held mainly by material and energy-intensive often subsidized industries that delayed the funds that could be spent on the financing of the sectors, which created the latest technology, machines and equipment, and which could ensure the sustainable development of the economy in the future.

However, the raw material intensive products "rescued" Ukraine while the European economy was developing dynamically. But it caused the sharp drop under the condition of the world financial recession because of the low competitiveness in the international markets.

The thesis that only the level of product innovation determines the ability of any country to develop successfully is not objectionable in world economics. The American economist with Ukrainian origin S.-S. Kuznets thinks that "The epochal innovation that characterizes the current economic era is the extended application of science to solve the problems of economic production" (Kuznets, 1966).

That is why the world's leading countries give priority to the science funding. However, the statistics show that in 2016 the spending of Ukraine on finance of scientific and technological projects at current prices increased by 16 times but their specific gravity in the gross domestic product during this period decreased to 0.66% (State Statistics Service Ukraine, 2016).

During 2000–2016, the specific gravity of Ukrainian enterprises spending on researches in the total financing of the innovative activity was 9-16% while decreased from 15% in 2000 to 10% in 2016. Thus, during these years, the companies spent only 3-5% of their research costs to buy new technologies. At the same time, 55-70% of the annual financial investment in innovative activity was directed to buy the machinery, equipment, and facilities connected with the innovations introduction. So, the innovative means were spent not on national science development finance but on the support of foreign companies (State Statistics Service Ukraine, 2016).

The *third reason*, which slows down the current economic development in Ukraine and makes the domestic products uncompetitive in the domestic and international markets, is the lack of state funding by the state and Ukrainian companies during the last twenty years of researches and innovative projects implementation.

The *fourth reason* is the non-conformity of the actions of the National Bank of Ukraine (NBU) and the Ukrainian government to the demands of the national economy.

In the second part of 2008, the global financial crisis spread across Ukraine. It caused a reduction in the rate of growth of gross domestic product (GDP) from 107.9% in 2007 to 102.3% in 2008. In August of the same year, the fall of production of industrial products happened. For example, in August 2008, the index of the volume of industrial products to the corresponding period of the previous year was 97.0, in September – 94.8, in October – 80.1, in November – 69.0, in December – 72.0%. In 2009, the crisis extended that caused the decline of GDP by 14.8%. The decline of the volume of produced industrial production was even greater – by 21.9%.

In 2010, Ukraine's GDP grew in comparison with the previous year by 104.1% and in 2011 – by 105.2%. That would indicate a stabilization of the national economy and its gradual recovery from the crisis. However, in 2012 this index increased only by 0.2%, in 2013 – 0%. In 2014, the dropping of Ukraine's GDP by 6.8% in comparison with the same period of last year was recorded. This indicates the entry of our country into the next phase of the financial crisis (State Statistics Service Ukraine, 2016).

It should be noted that in 2008-2009, most European countries came across a decrease in the rate of production of national GDP. However, to reduce the depth of the recession, they developed and implemented the measures to support domestic producers and consumers, which rely on the Keynesian theory.

4. Proposals to mitigate the effects of the economic crisis

After the crisis of 1929-1933, J. M. Keynes determined measures to be followed by countries to mitigate the effects of the economic crisis. The scientist considers that demand plays a key role in increasing of employment and production development and provides the increment of the revenue: "When employment increases, a real aggregate income increases too. The lack of effective demand will prevent the growth of production" and, to promote the economic development of the country, it is necessary to find levers that will increase the effective demand for consumer goods and investment demand, which are the components of the general public demand (Keynes, 1999).

So, the state by adjusting the total social demand may limit the uncontrolled growth of the national economy in a phase of growth and reduce its fall in the phase of recession.

John Maynard Keynes suggested his own mechanisms of ensuring the growth of effective demand as a determinant factor for employment increasing and growth in the national economy. They are:

– state regulation of the interest rate. To stimulate the manufacturers' interest in increasing the production, it is offered to lower interest rate on loans that will help to increase the gap between the expected profitability of the investment and the value of the loans or, in other words, the profits that remain in the company;

– the increase of state spending, investment, goods purchase and reduction of the tax load on businesses. The increase in the expenditure side of the budget should be offset by new tax revenues generated by increasing production and employment creation;

– increasing with the help of subsidies, grants, benefits, loans, the income of social groups, which are the largest group of consumers of products have the lowest rate;

– increasing with the help of state-funded public works facilities, stimulation to create new jobs by the employers, employment, and prevention of substantial unemployment.

These mechanisms were successfully used by many countries in the thirties of the twentieth century and are in use today and while they are criticized by the other economic concepts, better measures to reduce the negative effects of the recession are not proposed. However, analysis of the actions of national institutions, which are responsible for the development of the national economy during the crisis, shows that they ignored the recommendations of John Maynard Keynes working contrary to his offerings.

It should be noted that 2008 was characterized more than 20 percent inflation for Ukraine. That is why to decrease it the NBU and the Cabinet of Ministers of Ukraine began to restrict the money supply in circulation actively and raise interest rates even during the crisis. During the pre-crisis period, the money supply increased annually by 40-50% but in 2008 – 30%, and in 2009 in order to reduce the inflation, the money supply was reduced by 5.5% by the NBU. However, the NBU discount rate was increased from 8% in 2007 to 12% in 2008.

Thus, instead of reducing the mass of cash in circulation and increasing the interest rate in the period of economic growth, the NBU was following the actions during the recession, which were against the recommendations of Keynes, because it reduces the consumer demand and makes the credit facilities inapproachable for subjects of management.

As a result, the outflow of foreign financial resources to countries-residents increased by the reduction of the money supply and the volume of loans granted by domestic banks for residents. As a result, the credit supply of Ukrainian banks in 2009 dropped by 1.5% while domestic enterprises almost lost the opportunity to receive credit resources, the rate of which increased to 25-30%. As a result, the national economy during 2010-2015 is in stagnation and recession.

The well-known Ukrainian economist A. Chukhno says: "The crisis is one of the forms of economic development, during which outdated equipment and technology, production and labour are eliminated, space for the growth and consolidation of the new things is opened" (Chukhno, 2010). Thus, the scientists consider that the recession prompts the company to find ways to overcome the crisis, while stagnation "preserves" the problem.

5. Conclusions and suggestions

Thus, summarizing the abovementioned, we can draw a conclusion that the basis of past and present social and economic failures of Ukraine is the following: domestic officials' ignoring the changes that happened in the rules of development of economies in the twentieth century that are associated with the globalization and the monopolization of the global economy; the state's loss of the control over real economic processes in the country that led to shadowing of a large part of the national economy, deep stratification of the income of the population and active population outflow to other countries; insufficient funding of basic research and implementation of innovative projects by Ukraine and national enterprises; discrepancy of actions of the National Bank of Ukraine and the Ukrainian Government to modern needs of the national economy.

The abovementioned points are strengthened by the distrust of domestic entrepreneurs and people to Ukrainian government activities and the Ukrainian legal system. So, even the reduction of the tax load on taxpayers that takes place in Ukraine from 2011 after the new Tax Code adoption did not allow reviving the business activity in the country.

Thus, in order to ensure the rapid overcoming of the consequences of the recession and the rapid development of the national economy in order to bring it up to European standards and increase the standard of living of the population, Ukraine needs to take advantage of the experience of European integration of neighbouring countries and:

– to create a favourable legal and tax environment to attract foreign and domestic investment, to display the

entrepreneurial initiatives, to update the product and share the newly created revenue between state and objects of management, and various segments of the population equitably;
– to strengthen the law enforcing bodies activities in unshadowing of the national economy, limiting the output of domestic financial capital to offshore zone, monopoly and corruption in government;
– to provide the structural transformation of the costly and unprofitable industries, small and medium-sized businesses development and government support for start-ups;
– to reduce the social load on the payroll, to implement moderately progressive scale of enterprise income and personal income tax, and to monitor the wages of senior executives and everyone who receives it from the state and local budgets and expenditures for their maintenance closely;
– to increase state expenditures for the funding of basic and applied science, advanced equipment manufacturing and implementation of innovative projects;
– to realize a range of measures in order to make credit facilities available to producers and consumer. During a recession, it is necessary to lower the discount rate of the National Bank of Ukraine to zero, to increase the money supply in circulation, to provide a floating exchange rate of the national currency to convertible currencies and, as Keynes recommended, to maintain the inflation at 3-5% level.

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