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Ukraine's 272% Hyperinflation Rate Boosts Bitcoin's Prospects in Eastern Europe

By George Samman

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As Ukraine is currently experiencing the worst period of hyperinflation in the world as the government has imposed capital controls to stop its citizens from dumping the Hryvnia. This can potentially make cryptocurrencies the only viable safe haven for the embattled country's population.

"Yesterday a 62 year old man managed to get back his money from the bank (after 3 month of persistent attempts) and came to buy bitcoins. He does not trust the state nor the bank and is willing to take the risk of bitcoin volatility." -Michael Chobanian, the Bitcoin Embassy of Ukraine founder

Trouble in Ukraine

The situation in the Ukraine has gone from bad to worse. When a country passes Venezuela as the most inflationary place on the planet, things aren't going so well. According to government statistics, the official headline number on inflation is 28.5% year over year. However, Professor Steve Hanke of the Cato Institute disputes this:

"Using this figure and black-market exchange rate data that the Johns Hopkins-Cato Institute for Troubled Currencies Project has collected over the past year; I estimate Ukraine's current annual inflation rate to be 272 percent – and its monthly inflation rate to be 64.5 percent. This rate exceeds the 50 percent per month threshold required to qualify for hyperinflation. So, if Ukraine sustains its current monthly rate of inflation for several more months, it will enter the record books as the world's 57th hyperinflation episode."

Apparently the Ukrainian government has completely under reported the numbers to further its own agenda to avoid mass panic. Sound familiar? Unfortunately, it is bit too late for that as the Ukrainian currency, the hyrvnia, has dropped 70% since the beginning of 2014.

In previous articles, the causes of hyperinflation have been defined. In the case of Ukraine, it has been caused by systematic corruption, a war with its pro-Russian secessionist eastern regions, which has destroyed a lot of its factories and caused the country to lose a quarter of its industrial capacity. This resulted in a huge output gap and a rapid increase in the money supply to help finance its ongoing war.

Russia is also its largest trading partner so that does not help matters. Ukraine is running massive deficits and as no revenue coming in, the beleaguered nation is on the brink of default.

Capital controls

The government has attempted to fix the exchange rate in an attempt to quell the panic and a run on the banks. This has led to Ukraine's minimum wage to be approximately US$42.90 per month, which puts it lower than Ghana or Zambia, the RIA reports. This has led to what resembles typical hyperinflation:

"Food prices among producers rose 57.1 percent, with the price for grains and vegetables rising 91 percent from January 2014 to January 2015, while the official inflation rate over the period totaled 28.5 percent. Meanwhile, Ukrainian consumers responded to economic difficulties by cutting their spending in hryvnias by 22.6 percent, which amounts to an almost 40 percent decrease in real consumption."

This rapid rise in inflation and collapse in the currency has led Ukrainian President Poroshenko to take extreme actions and to tighten capital controls even more, which the government has since dialed back slightly.

When the Hyrvnia was in free fall Wednesday February 25, the central bank banned banks from buying currency on behalf of their clients for the rest of the week. This was later repealed but it is still near impossible to exchange currency at the banks. In February alone, this has led to a massive spike in the USD/UAH rate as the US dollar continues to surge as people are looking for safe havens.

“Even though officially the foreign exchange limit is 3,000 UAH (hrynvias) per day you still can't buy or sell foreign currency in the bank,” said the founder the Kuna Bitcoin Agency and The Bitcoin Embassy of Ukraine, Michael Chobanian to CoinTelegraph. “They will not sell you any. So there is practically no liquidity.”

He added:

“Exchange still works but huge obstacles have been put up. It will take a minimum of 4 days if you want to buy USD (for a company or an importer). The average person does not have access to interbank exchange.”

This has led to massive growth in the underground economy. The IMF estimates that Ukraine's underground—and non-tax-paying—economy is as much as 50 percent of GDP. This has only compounded Ukraine’s problems as government revenues have declined massively.

Exchange kiosks on the streets in Kiev were selling limited amounts of dollars for 39 hryvnias - around 20 percent higher than the rates advertised in the windows of commercial banks where dollars were not available.

Even regular citizens in the country are increasingly turning to bitcoin as a safe haven according to Chobanian, who explained:

“[N]owadays I have clients who aren’t even tech savvy looking to buy bitcoin. Yesterday a 62 year old man managed to get back his money from the bank (after 3 month of persistent attempts) and came to buy bitcoins. He does not trust the state nor the bank and is willing to take the risk of bitcoin volatility. The old man said ‘with bitcoin I am sure that I will always get at least something. With the bank I almost lost everything.’”

As is always the case in hyperinflationary episodes, people are trying to get rid of hyrvnia as soon as they get them since they will be worth less tomorrow. The price of gold has also spiked in UAH terms:

Crypto’s time to shine

In countries with persistently high inflation rates, such as Argentina and now Ukraine, bitcoin has a real use case. Particularly, when capital controls are introduced making it almost impossible to access other currencies and asset classes.

For high net worth individuals in these countries, there are ways to trade hard assets like real estate and precious metals for bitcoin, which can easily be sold during hyperinflation as the local currency devalues rapidly. This allows you to bypass banks and capital controls, but the problem remains for the rest of citizenship and how they can get bitcoin without having to trade their worthless fiat into something else just to get bitcoin.

Unsurprisingly, Ukraine’s government issued a warning against cryptocurrencies back in November, 2014. However, this has not disrupted the operations of Bitcoin businesses in the country. “The announcement does not affect my business in any way,” Chobanian told CoinTelegraph back in November. “This is a simple runaround. Based on the contents, it’s clear that the NBU (National Bank of Urkaine) does not understanding the situation.”

Meanwhile, the price on LocalBitcoins in Ukraine has reach an asking price of as high as ~US$413.65 (10,947.19 UAH) per bitcoin - nearly double the market price – pointing to considerable demand for the cryptocurrency, which may also be partially responsible for the latest price increase.

Thus, a real opportunity exists for both cryptocurrency and Ukraine's citizens who are trying to dump worthless fiat that no one wants in exchange for bitcoin.

And while friction undoubtedly exists, this may be a perfect time not only for cryptocurrency to flex its muscles in the embattled country, but also for Bitcoin businesses and exchanges like Kuna Bitcoin agency, who may offer the only viable option to retain people's savings.