INSTITUTE FOR ECONOMIC RESEARCH AND POLICY CONSULTING

Year 2010: Economic Summary for Ukraine

Beginning of reforms

EXECUTIVE SUMMARY:

- The cooperation with the IMF was reloaded. On July 28 the IMF Executive Board approved a 29-month SDR 10 billion (near USD 15.15 bn) Stand-By Arrangement for Ukraine. The initial disbursement equivalent to USD 1.89 bn was available immediately.
- After sharp drop in 2009, real GDP grew by 4.2% in 2010 primarily due to increase in real private final consumption. Net exports made negative contribution to real GDP growth at 2.7 p.p.
- Industrial production grew due to recovery of export-oriented sectors.
- Agricultural performance was supported by further growth of livestock sector, while crop production was lower than in 2009.
- The gas market reform was initiated in 2010 with the approval of the law on natural gas market. Moreover, the gas tariffs for population were increased by 50% in August.
- The National Regulatory Commission for Public Utility Markets was established as a independent regulatory market to start operation in 2011. It will be responsible for setting tariffs, which were defined by local authorities before.
- Current account deficit widened to USD 3.0 bn. It was covered by financial account surplus.
- Population welfare improved in 2010. Unemployment rate (ILO) reduced, while real wages grew by 10.2% in real terms.
- The Government succeeded to conduct several fiscal reforms. The Tax Code was approved combining all legislation on tax system into one document. Besides, new version of the Budget Code was approved. The Parliament also approved a long expected law on public procurement.
- The law on unified social contribution was approved meaning that starting 2011 companies will pay only one social security payment instead of four. The Pension Fund was defined as an administrator of this contribution.
- The Pension Fund's gap remained high being financed by the direct central fiscal transfer as well as loans provided by the State Treasury.
- State borrowings remained major source of fiscal deficit financing. As a result, state debt reached USD 54.3 bn or 36% of GDP in 2010.
- The Ukrtelecom was *de facto* privatised in 2010, even though receipts were transferred to the budget only in 2011.
- Consumer inflation returned to single digits.
- UAH/USD interbank exchange rate remained generally stable in 2010.

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IMF: Cooperation reloaded

The economic crisis resulted in active role played by the IMF in Ukraine's economy from end of 2008. The IMF loans during 2009 helped Ukrainian Government to fulfil its liabilities in time, including servicing of external debt. High fiscal pressure in 2010 pushed new Government to look for the continuation of cooperation with the Fund.

The IMF mission returned to Ukraine in the end of March 2010 to continue negotiations after terminating the Stand-by program in autumn 2009. As in 2009 the major controversial point of new round of talks was fiscal consolidation. One of the major concerns of the IMF was an issue of fiscal sustainability in Ukraine, in particular, the size of social standards to be envisaged into the State Budget Law for 2010. However, as consensus was not reached, the IMF did not approve disbursement of the next instalment of the loan.

In June talks continued on approval of new Stand-by Arrangement, rather than restoration of the previous one as the tasks faced by Ukraine have changed. On July 28 the IMF Executive Board approved a 29-month SDR 10 billion (near USD 15.15 bn) Stand-By Arrangement for Ukraine. The initial disbursement equivalent to USD 1.89 bn was available immediately. Out of that instalment USD 1.0 bn was transferred for budget purposes.

The approval of new Arrangement became possible due to the approved by Ukrainian Government measures. The State Budget 2010 was sequestered (see *Fiscal Policy*). The Law on the Regulation of the Natural Gas Market (see *Energy Policy*) was approved. Besides, the gas tariffs for population were raised by 50% since August 1. The amendments to the NBU law envisaged higher independency of the NBU and gradual implementation of the inflation targeting.

Key objectives of new Program were consolidation of public finance, restoration of banking system soundness, and more robust monetary policy. The signed Memorandum defines targets for the general government deficit at 3.5% of GDP in 2011 and 2.5% of GDP in 2012. The public debt is to decline to 35% of GDP by 2015. The continuation of the pension reform is required as one of the measures for fiscal consolidation. The retirement age for women is expected to increase to 60 (from current 55). The minimum insurance and working records are also to be raised. The further reforms to modernise the gas sector are also expected. The Government promised to increase further the gas tariffs for heating-generating companies and population to ensure elimination of the Naftogaz's deficit already in 2011.

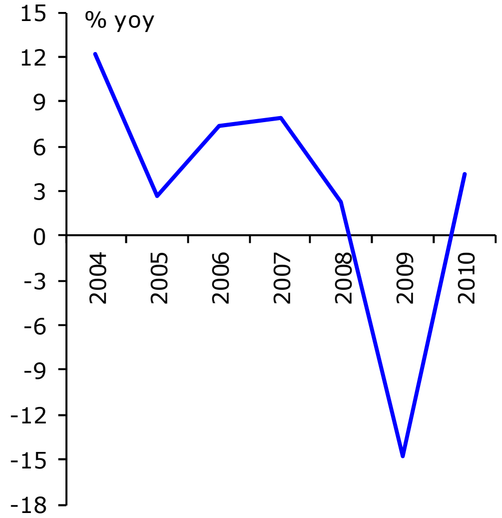
The IMF mission returned to Ukraine in November 2010 for scheduled quarterly review of the arrangement. The mission concluded that Ukrainian performance was in line with the program objectives. In the end of December, the Executive Board completed the first review of country's economic performance under the program supported by a Stand-By Arrangement. The IMF immediately disbursed USD 1.5 bn to Ukrainian authorities. From this amount USD 1.0 bn was allocated to budget improving fiscal positions of the Government for the beginning of 2011.

Overall, Ukraine has become the second largest borrower of the IMF after Romania. The continuation of cooperation provided Ukraine with additional funds for debt redemption as well as opened international capital markets for Ukraine.

GDP: Modest recovery in 2010

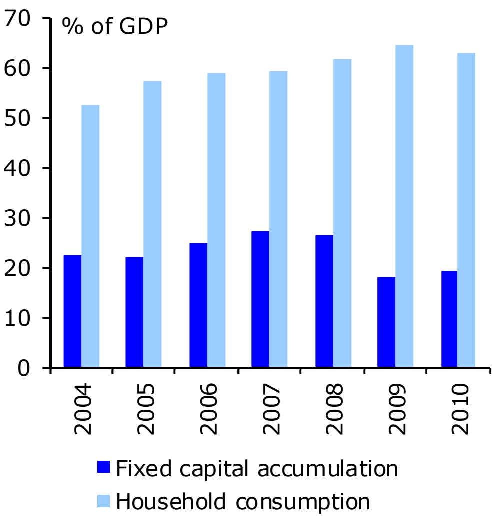
After sharp drop in real GDP in 2009 (at 14.8%) economy started recovering in 2010. External demand for Ukrainian products increased, but remained weak and unstable throughout the year. Limited banking lending restricted growth of investments. Overall, real GDP grew by 4.2% in 2010.

Real gross domestic product



Source: Derzhkomstat

Structure of gross domestic product



Source: Derzhkomstat

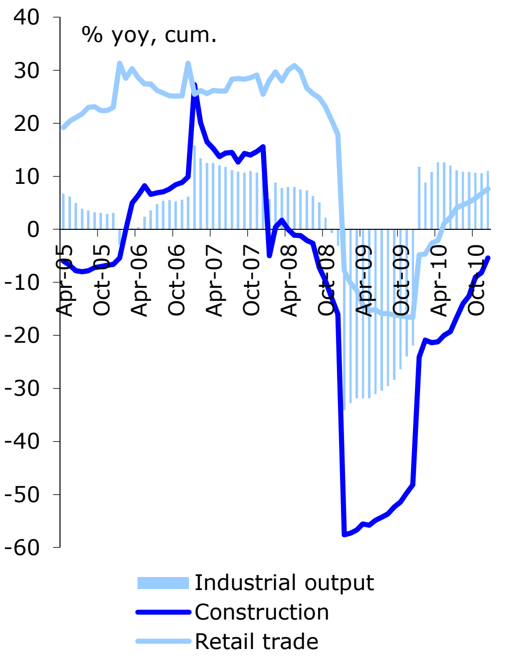
Real exports and imports

Source: Derzhkomstat

On demand side, the major contributor to growth was real private final consumption, which increased by 7.0% due to sharp recovery of real disposable income (see *Wages and income*). The debt burden on households also declined, thought, maintained negative contribution to the consumption growth. Besides, households accelerated net purchases of cash foreign currency. Real gross fixed capital accumulation grew by 4.9% due to fast growth in the second half of the year. However, investments were likely overstated as simplified registration rules led to sharp increase in reported residential construction including of houses completed in previous years. Increase in consumption and moderate recovery of investments resulted in real imports growth (at 11.1%). At the same time, exports increased at much slower pace (by 4.5%). As a result, net exports had negative contribution to the real GDP growth at 2.7 p.p.

On production side, manufacturing contributed the most to the economic recovery. In particular, real gross value added (GVA) in manufacturing sectors grew by 4.5%. Extractive industries increased GVA by 3.3%. Higher production and consumption stimulated GVA growth in trade and transport and communication (at 4.0% and 5.1%, respectively). At the same time, GVA in construction decreased by 1.7% recovering in the second half of 2010. The agriculture also demonstrated decline in GVA (by 1.3%) due to worse harvest, which was only partially supported by growth in livestock production (see *Agricultural output*).

Real sector trends



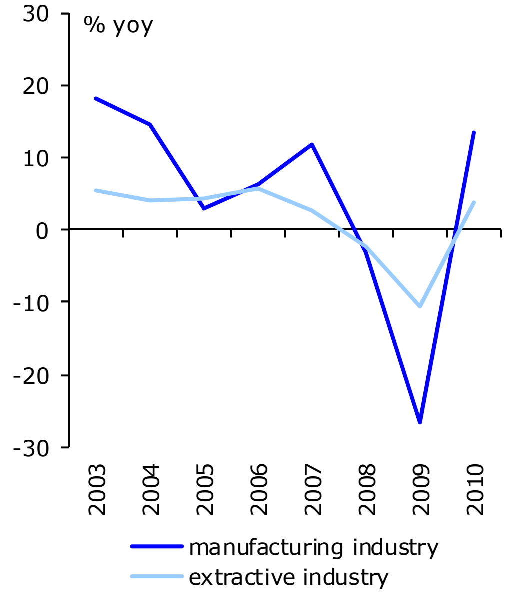
Source: Derzhkomstat

Investments: Continued stagnation in 2010

Investments remained stagnant in 2010 being suppressed by economic crisis and pessimistic risk perception by majority of investors. Revenues downfall, expensive debt servicing and stagnating stock market forced business to suspend large investment projects in modernization of production facilities. As a result, real gross fixed capital accumulation increased by 4.9% in 2010, thus, mainly preserving at crisis level.

Real gross fixed capital accumulation decreased the most in commercial real estate and infrastructure objects. The construction was largely frozen or insufficient due to low funding both from state and private sources. According to Derzhstat, real gross fixed accumulation in other than commercial real estate was increasing over 2010. Large construction companies continued to suffer from liquidity squeeze. On the contrary, residential construction revived and increased in 2010 reaching 49.6% growth. The revival mainly happened at the expense of individual construction supported by increased households' incomes and low statistical base. Yet other explanation is methodological, as since 2010 private construction without legal permission has been included into official statistics. Meanwhile, large construction companies continued to suffer from liquidity squeeze.

Growth of industrial output



Source: Derzhkomstat

Real gross fixed capital accumulation in machinery and equipment was weak in 2010. Large industrial companies had frozen the large-scale investments and concentrated on minor improvements of production facilities. In 2010 growth of real investments in machinery and equipment was multidirectional and unclear. It was changing from 7.8% yoy increase to 11.0% yoy decline over two quarters and then increased by 13.2% yoy in the third quarter. Overall in 2010 investments in machinery and equipment grew by 14.5%.

According to the sectoral structure of investments in fixed capital (which is a narrower category than gross fixed capital accumulation), the most rapid contraction in 2010 was observed in manufacturing industry (by 9.5%), retail trade (by 25.2%) and financial services sector (by 21.3%). Investments in air service fell by 29.5% over the same period. On the contrary, land transportation and operations with real estate sector accelerated investments in fixed capital by 55.7% and 32.2%, respectively, favoring from revenues increase.

Industrial output: Partial recovery after the crisis

In 2010, industrial production partly recovered primarily thanks to export-oriented branches. Still, the year was quite difficult for producers, and physical volume of industrial output did not reach pre-crisis level. The recovery was suppressed by external demand volatility, caused by changeable investment activities in developing countries funded through public sources. In Ukraine, uneven recovery of domestic demand and limited bank crediting became other restrictive factors for industrial output growth.

According to the Derzhkomstat, real industrial output grew by 11.2% in 2010. Machine building and chemical industry became the leaders of recovery with output increase by 36.1% and 22.5%, respectively. Output in metallurgy grew by 12.2% limited by unsteady demand on world commodities markets. The weakest recovery was registered in food industry and in non-metallic goods production that expanded their output by 3.2% and 8.5% in 2010 constrained by weak domestic demand.

Production of vehicles was the best performing sector, which output expanded by 61.9% in 2010. This growth was associated with rapid increase in external orders for railcars and trucks from developing countries, mainly the CIS, against the background of large public investments into infrastructure in those countries. External demand also fueled growth of other sub-sectors of machine building, which output increased by 21.1% on average in 2010.

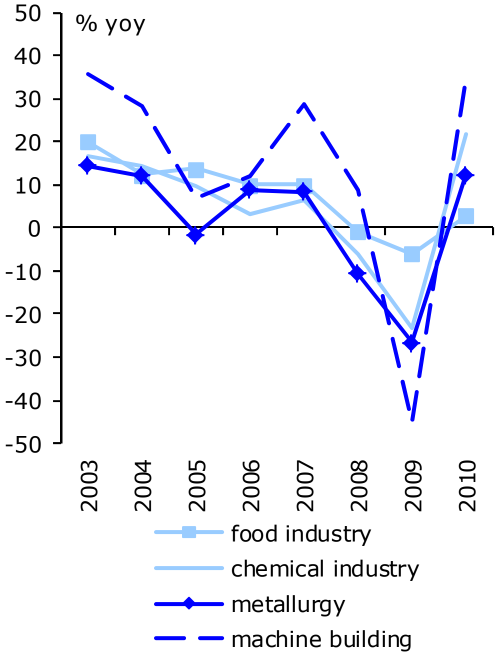
Chemical industry benefited from growing demand on nitrogen fertilizers at the world market, and from subsidized price on natural gas being main input for fertilizer production. Growing prices and stable costs resulted in growth of production in chemical and petrochemical products at 26.6% and 10.1% in 2010, respectively.

Year 2010 was quite tough for metallurgy. Recovery of traditional markets for Ukrainian steel products (Far East, North Africa and the EU) was not as strong as expected, and national steel companies had to switch to highly competitive Chinese market. The latter was heavily dependent on public investments in infrastructure construction; thus, demand for steel products was very unstable. Still, steel prices growth, depreciated national currency and intensive cost cutting allowed Ukrainian steel producers to withstand competition, and increase sales and capacity utilization.

World deficit of iron ore was the major supportive factor for extractive industry. Expansion of exports allowed increasing iron ore extraction by 14.8% in 2010. On the contrary, extraction of fossil fuels continued to fall and decreased by 3.1% due to insufficient investments in development of new deposits.

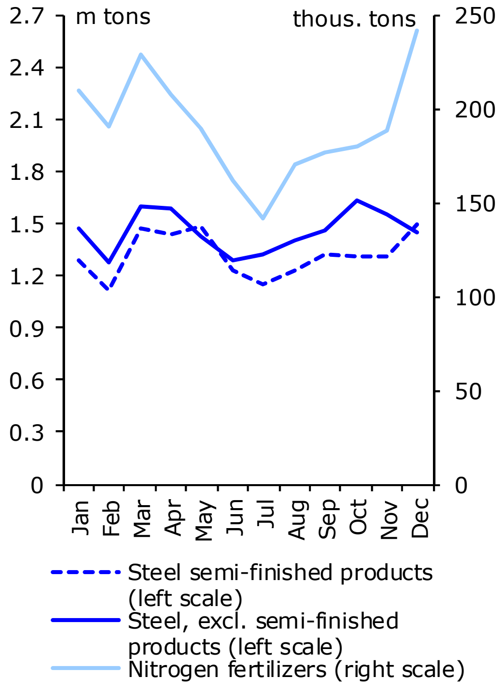
Weak internal demand resulted in moderate growth of domestically oriented industries. Food production (excl. tobacco) increased by 4.5%, while strong tax pressure led to 10.4% contraction in tobacco products output. Collapse of industrial and infrastructure construction resulted in moderate growth of construction materials output, primarily demanded for individual construction purposes by households.

Growth of output in key industrial sectors



Source: Derzhkomstat

Production of major export commodities in 2010



Source: Derzhkomstat

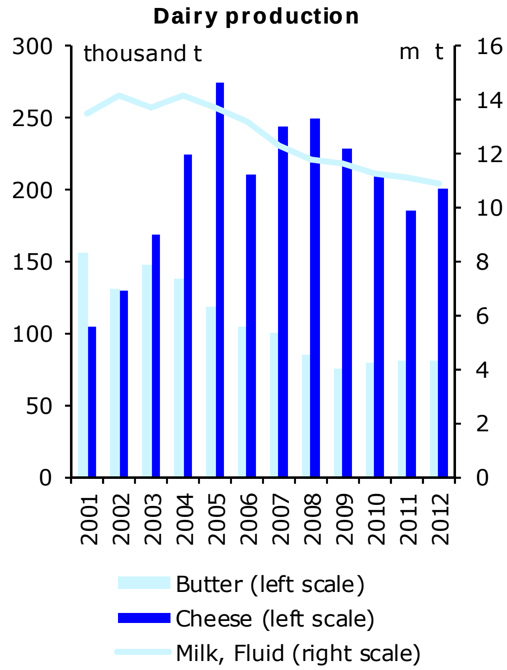
Agricultural output and trade: Overall decline despite the uphold in livestock

Agricultural performance somewhat deteriorated in 2010 compared to 2009. Positive developments in the livestock sector compensated a bit for a worse harvest this year, resulting in a mild total agricultural output decrease by 1.5% in 2010. Structurally, the major decline occurred in the performance of households' subsidiary farming, leading to increased output share of agricultural enterprises.

Ukraine harvested 39.3 m t of grains and pulses in 2010, which is about 13% less than the year before. The main reasons for this decline were unfavorable weather conditions and a slight decrease in harvested areas (about 3%). In the sugar sector, on the contrary, a high domestic demand and low stocks-to-use ratios, combined with expected high world sugar prices and protective government policy, resulted in a 37% increase in sugar beet output in 2010 to 13.8 m t. In the oil seed sector, a growing world demand for vegetable oils, low stocks-to-use ratios, and underloaded capacities of the Ukrainian crushing industry basically resulted in 6% growth of sunflower seed production (6.8 m t) and increased soybeans output by 61% (1.7 m t). The largest share of soybeans is consumed domestically in the growing poultry and swine sectors. In the rapeseed sector, on the contrary, the output and exports dropped by 22% and 19%, respectively. Competition from other oil crops as well as new certification requirements for rapeseed imports in the EU are called as primary driving forces behind such a development. The combined effect in crop production is a decrease by 4.7% in 2010.

Despite an overall decrease in crop exports, Ukraine retains leading positions in the world oil crops trade. Grain exports, however, fell by about 41% mainly because of export restrictions in Ukraine that were introduced in the fall 2010 and have been prolonged until the end of March (see *Agricultural Policy*).

Animal production increased by 3.2% in 2010. In particular, agricultural enterprises demonstrated an increase of 8.2% in output and households reduced production by 0.5%. Households, however, continue to dominate in the meat (except poultry) and milk sectors. They accounted for 66% of the livestock, 55% of pigs, 83% of goats and sheep and 46% of poultry heads in Ukraine. The country remained a net importer of livestock and pork meat. Increasing poultry and eggs production in large agriholdings that provide better quality of products and, therefore, better export opportunities resulted in poultry export increase by 77% in 2010. However, it still remains insignificant since the majority of the produced in the country poultry meat is consumed domestically. The dairy exports remain insignificant due to the low quality of raw milk in households. In 2010 it declined by further 9%.

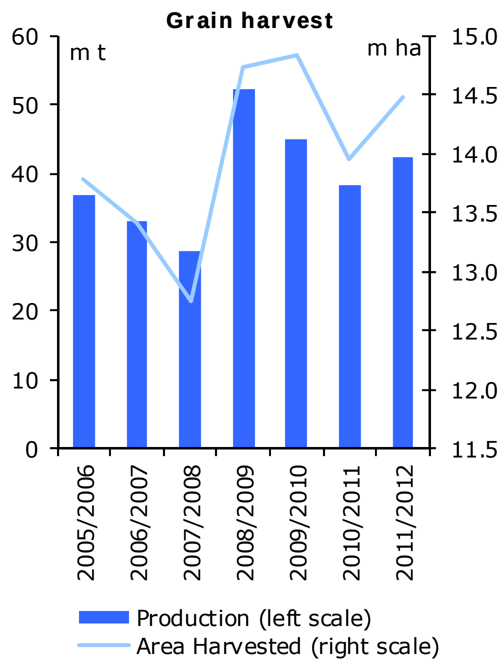


Source: USDA data as of 19.12.11

Agricultural policy: Simultaneous pushing gas and brakes pedals

In 2010, Ukraine's agricultural policy continued simultaneous pushing gas and brakes pedals. Despite the Government's efforts to streamline economic policy framework in the sector embedded in the taxation system reform and new VAT refund schemes, hand steering proliferated in some sub-sectors reducing their competitiveness.

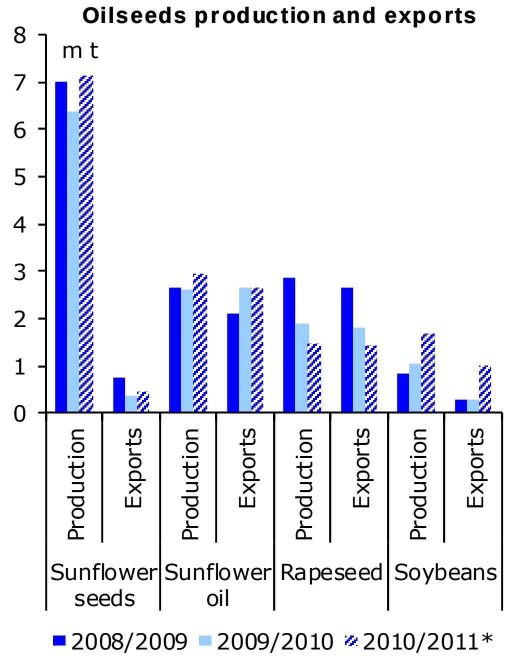
Budget outlays for agriculture increased by roughly 10% in 2010 compared to significantly declined funds of 2009 and reached about UAH 7.8 bn. Amber box support measures totalled to UAH 1.6 bn, which is well below the maximum support level envisaged under the WTO commitments.



Source: USDA data as of 19.12.11

Despite above than average harvest of grain (39 m t), export restrictions were introduced in the beginning of the marketing year 2010/11. First, exporters were exposed to tougher export regulations, mainly in the form of protracted grain quality checks and delayed shipments in the ports. This continued until the Government formally introduced grain export quota 2.7 m t[i], including wheat – 0.5 m t, barley – 0.2 m t, corn – 2.0 m t, rye and buckwheat – 1 thousand t each, until the end of 2010, officially because of low domestic supply of grain. Since the quota is well below Ukraine's grain export potential in 2010-2011 marketing year, this decision decreased domestic grain prices by USD 50/t on average. The resulting rough estimate of losses, excluding entailed losses to exporters and to the investment attractiveness of the sector, amounts to USD 1.9 bn[ii] as farmers were not able to benefit from favourable world prices.[iii] It is twice as high as the total budget outlays to agriculture (USD 1.9 bn vs. USD 0.98 bn, respectively).

The Government cancelled the possibility of in-kind VAT refunds for exporters and offered to use VAT obligations.[iv] Further more radical VAT reforms are envisaged in the new Tax Code, namely the exclusion of grain exporters from VAT for the period from July, 2011 till January, 2014.[v] The whole special VAT regime is scheduled to be modified: since January 2011, agricultural companies would accumulate the VAT funds on special accounts and would be no longer granted any VAT privileges staring from 2018. Milk and meat processors, in turn, will have to pay VAT sums to the budget and not to the suppliers of raw milk and meat as before. Together with adding new taxes not included into fixed agricultural tax FAT – namely, ecological tax and land tax for parcels not used in agricultural production – and more stringent eligibility requirements for FAT payers, these measures might translate into higher tax burden for the sector.



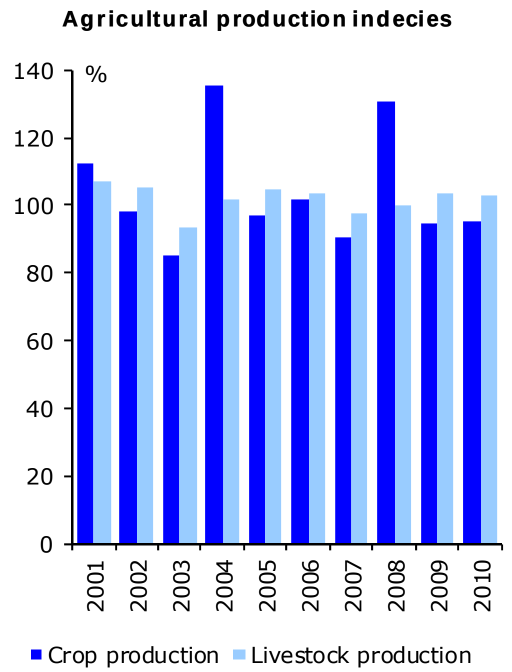
Source: USDA data as of 19.12.11

Energy policy: Reaching the balance on gas market

Imported gas prices. After the Presidential elections and new Government formation the priorities of state policy on gas market have been shifted towards obtaining the discounts on import of Russian natural gas and increase of domestic gas prices.

On April 21, according to adopted amendments to gas agreement with Russia, Ukraine received the discount on imported natural gas at USD 100 per thousand cm over the following 10 years starting from the second quarter of 2010. Instead, the Russian Black Sea Fleet stay in Sevastopol naval base will be prolonged for another 25 years preserving the same annual USD 100 m rent fee. It allowed to retain the weighted-average price of imported gas at USD 258 per thousand cm (tcm) and, thus, to support gas-dependant chemical and steel industries.

Domestic gas tariffs. The National Electricity Regulatory Commission (NERC) approved resolution about increase of gas prices for population and local heat generation companies by 50% starting August 1, 2010. As a result, basic[vi] gas price for households and local heating companies increased to UAH 725 and 1309 per tcm, respectively. Tariffs for industrial consumers and budget entities were also increased by 9.8% to UAH 2187.20 per tcm starting August 1, 2010. At the same time, the Government continued to maintain the privileged gas price for nitrogen fertilizer producers. That price grew only by 3% to UAH 1633.30 per tcm in 2010.



Source: Derzhkomstat

Naftogaz. At the beginning of the year the state monopolist on the gas market – NJS Naftogaz of Ukraine – had been suffering from severe liquidity crunch. The company's cash flow deficit was primarily incurred by losses from gas sales to local heat generating companies at discounted prices while the price of import of Russian gas reached more than USD 300 per thousand cubic meters (cm). Simultaneously, local authorities failed to compensate losses to heat generators in 2009 that resulted in the highest indebtedness of the latter before Naftogaz at the beginning of the year. It reached UAH 3.65 bn as of February 19, 2010 and was being the major reason of Naftogaz huge liquidity gap estimated at UAH 10 bn in 2010. In response, the Government preserved high volumes of direct budget support or UAH 3.4 bn in State Budget of 2010 and continued to provide loans to the monopolist through the state banks.

Despite liquidity problems, increase of domestic gas tariffs and granted enterprise profit tax privilege allowed to slightly improve the profitability of NJS Naftogaz in 2010. According to non-consolidated financial statements[vii] for 2010, the company demonstrated net loss of USD 1.5 bn comparing to USD 2.8 bn of net losses in the previous year.

Conflict with RosUkrEnergo. Additional problem for gas market stability was caused by a conflict over the former gas intermediary in Ukrainian market – RosUkrEnergo AG. At the beginning of the year the company initiated a trial against Naftogaz in the Arbitration Institute of the Stockholm Chamber of Commerce. The latter decided to satisfy RosUkrEnergo claims. According to two decisions that have later been recognized by the Supreme Court of Ukraine and agreed by trial parties, NJS Naftogaz was obliged to return gradually 12.1 bn cm[viii] of natural gas to RosUkrEnergo AG, while RosUkrEnergo AG will pay USD 1.7 bn of its debt to Naftogaz. Thus, Naftogaz will avoid the reputation losses but this deal will add an additional financial pressure on the company as it will be required to replace this gas by new one, on higher prices.

Oblgases. Regional gas distribution companies (oblgases) have been again separated from Naftogaz. On July 5, 2010, the Cabinet of Ministers cancelled its previous decision[ix] about transferring assets of these companies to Naftogaz. At the same time, the tariffs for gas transportation and supply have also been increased to UAH 142.3 per tcm for transportation and UAH 41.3 per tcm for supply that is expected to make this business profitable in the next year.

Gas market reform. In mid-2010, long-awaited legislative reform of gas sector has begun. On July 8, the Parliament approved Law "On principles of operations on the natural gas market"[x] which set the principles and schedule of national gas market reform. By this law Ukraine declared an intention to set up the competitive gas market structure on the basis on the EU appropriate legislation[xi] and conduct vertical unbundling of Naftogaz which involves separating the transportation, distribution and supply activities of the monopolist starting 2012. The implementation of declared principles is expected to overcome existing harmful cross-subsidized pricing and make the gas market more attractive for investments.

In December Ukraine made another step towards harmonization of energy legislation with European one after accession to European Energy Community. The Parliament ratified the Protocol of Accession to Energy Community[xii] according to which Ukraine has taken the liabilities to adopt legislation on regulation of gas and electricity markets according to the EU standards. It is expected that modernization of national legislation will create the possibilities for Ukrainian energy providers to supply the energy recourses directly to European markets. Moreover, more transparent structure and regulation procedures will stimulate the investments by European energy companies into national gas and electricity markets infrastructure.

GTS modernization and gas supply diversification. In 2010, Ukraine continued to seek external investors for modernization of the gas transportation system (GTS) and development of gas deposits, and possibilities to diversify the supply of natural gas.

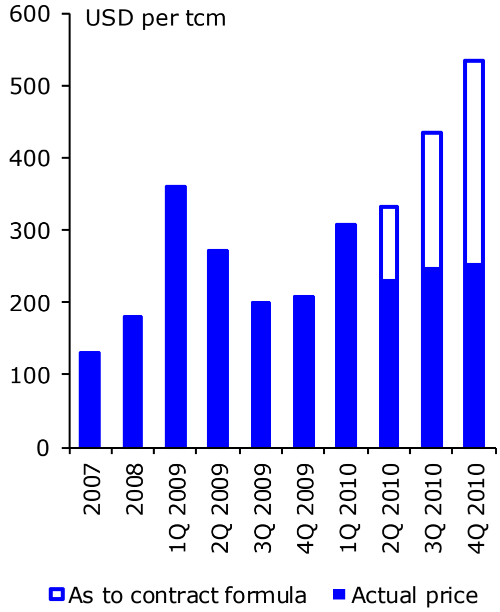
In the second half of 2010, Ukraine initiated a series of negotiations with the EU and separate European countries (including Germany and France) concerning the investments in modernization of GTS. As a result, the international organizations (namely, the World Bank, the EBRD and EIB) agreed to make the first tranche of investments in Ukrainian GTS modernization in mid-2011 at the total amount of USD 308 m in framework of previously signed Brussels declaration.

The similar negotiations with Russia were not so successful. Ukraine refused the proposal to establish the joint venture with Russian Gazprom with an ownership of Ukrainian GTS as one of the stakes in exchange for investments. The agreements with Russia were signed on 5-year warranty of gas transit through Ukraine at annual volume of 112 bn cm that made investments in GTS more predictable and on the joint activity with Russian Gazprom on gas deposits extraction in the Black Sea and from coal beds methane in Donbas.

Meanwhile, Government actions showed that Ukraine intends to invest in GTS modernization and infrastructure for gas supply diversification independently. In 2010, Naftogaz almost doubled investments in GTS maintenance and renewal to UAH 1.75 bn and declared about plans to increase investments to UAH 3.1 bn in 2011. Certainly, it is much less than the required USD 6.5 bn till 2018 estimated by the Ministry of energy and coal industry but it would strongly motivate the external investors to put forward strict investment proposals in the nearest future.

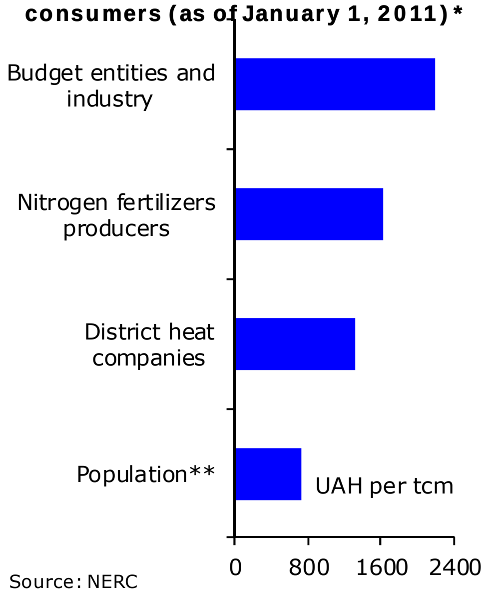
Also, Ukraine set up state enterprise on construction of the first liquefied natural gas (LNG) terminal in Odesa in January 2011 with planned capacity of 10 bn cm and started the talks with LNG

Price on imported natural gas



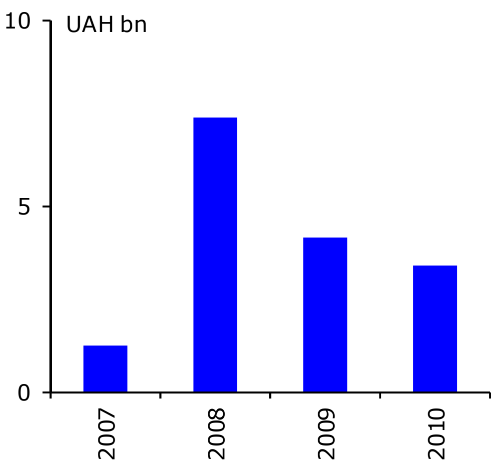
Source: NJS 'Naftogas'

Gas prices in Ukraine for different consumers (as of January 1, 2011)*



Source: NERC
* Prices excluding VAT, extra charge, and transportation & supply costs
** Average price

Fiscal compensation to NJS 'Naftogas'



Source: Treasury reports

suppliers. It is expected that success of this project with total investment volume of USD 1 bn and increase of own gas extraction (including from unconventional sources) would decrease Ukraine's dependence on pipeline gas import from Russia.

Electricity. In 2010, new auction mechanism of electricity exports[xiii] defined the landscape of electricity exports. Despite set procedures that foresee competition between electricity traders new rules can be estimated as uncompetitive. The electricity grids operator – state company NEC Ukrenergo – has been blocking applications for export capacities of companies other than affiliated with corporation DTEK. With the background of falling electricity supply to Western Europe due to shortfall of electricity prices in this region distortion of competitive mechanism made export of Ukrainian electricity to Europe unprofitable.

The NERC continued to increase electricity tariffs for domestic industrial consumers towards cost-covering level. Tariffs were increased by 21% in 2010. The moratorium on tariffs increase for steel and chemical producers was cancelled. At the same time, electricity tariffs for population remained unchanged which preserved financial pressure on state energy generating companies.

In nuclear energy sector, Ukraine has kept the existing scheme of nuclear fuel supply for Ukrainian nuclear power plants (NPP). Energoatom and Russian nuclear fuel producer TVEL signed an agreement on renewal of the current supply contract. Accordingly, Russia will remain the major supplier of nuclear fuel for the next 20-25 years that will made the modernization plans in nuclear sector more definite in long-term.

Moreover, TVEL won the tender and became the major contractor for construction of a new nuclear fuel plant in Ukraine and new power energy units for Khmelnitska NPP. It will further promote the plans of creation of closed nuclear fuel cycle production in Ukraine and increase the share of NPP in total electricity generation.

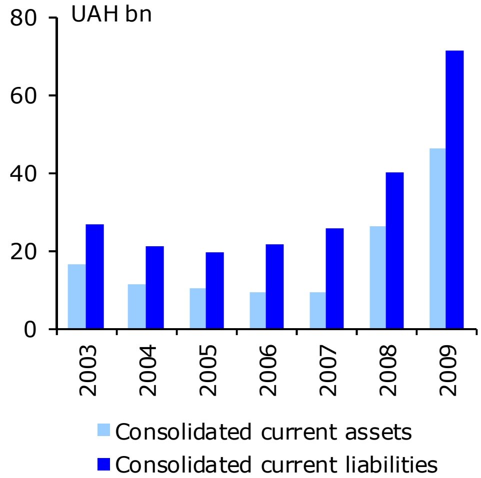
Renewable energy. Corporation DTEK started the first large-scale investment project in renewable energy sector in Ukraine within the framework of so-called "green tariff", which envisages the privileged price for electricity generated from renewable sources. The company announced plans to build the largest wind energy power plant in Ukraine in 2011 with total installed capacity of 200 MW that is twice higher than existing capacity of all already installed units (about 90 MW). If successful, it will become the positive signal for investors to increase their participation in renewable energy market in Ukraine.

Transport: "Creeping" improvements in transport regulation

Tariffs. In 2010, the Ministry of Transport and Communications (MTCU) abandoned using tariffs as a tool of financial support of state-owned transport companies. Instead, the Ministry strived for stimulation of transport flows that dropped after the crisis. In January, it introduced 20-50% discounts for services provided by Ukrainian ports for foreign cruise ships.[xiv] In March, it prolonged 18-50% discounts set in 2009 for transit freight services in ten ports until December 31, 2010.[xv] Handling of transit cargo in containers[xvi] as well as berthage for oil transit[xvii] also became substantially cheaper. Since relatively high railway freight tariffs limited potential positive impacts of these decisions, railway authorities also introduced significant (15-50%) discounts for transit freight transportation.[xviii] However, Ukraine has been far behind in the regional race for transit freight attraction and infrastructure improvements. So, those measures were timely but insufficient. Transit freight handled by Ukrainian ports as well as freight transit by rail continued to fall in 2010. To support the sector discounts for transit have been prolonged for 2011.[xix]

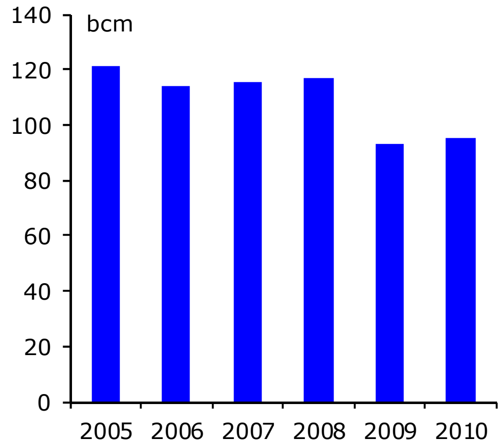
In addition to reducing rates, the MTCU stimulated competition in the sector by calling off several competition-distorting decisions. First, in July 2010, tariff preferences for metallurgy and chemical industry

NJSC Naftogaz Ukrainy solvency



Source: NJSC 'Naftogaz Ukrainy'

Natural gas transit through Ukraine to Europe



Source: Derzhkomstat; NJC 'Naftogas'

provided in late 2008 were finally abolished,[xx] and rail tariffs for these two sectors were increased after being frozen for almost 2 years[xxi]. Second, from January 1, 2010 the Government called off the practice of setting minimum tariffs for freight transportation by road.[xxii]

The only exception in pro-competitive tariff policy was an increase in air navigation charges. In October 2010, unit rates of charge for route services increased from EUR 37.26 to 45.56, and for approach and aerodrome control – from EUR 5.88 to 7.56.[xxiii] International air organizations such as IATA, EUROCONTROL, and AEA actively protested against these changes as allegedly unjustified. It was stated that new rates take into account high profit margin, when such practice is absent in the EU at all. Although rates charged by Ukraine are not the highest in Europe, this decision could become an issue in the EU-Ukraine negotiations on Common Aviation Area.

Infrastructure. Transport companies, in particular state monopolies, continued their vicious practice of accumulating debts without noticeable improvements in their services.

After the failure to pay back the second USD 110 m instalment out of USD 550 m syndicated loan to Barclays Bank PLC in 2009, the Ukrzaliznytsia (UZ) restructured the debt in May 2010. Maturity of the loan was extended by five years. In August, UZ again failed to pay USD 110 m. This failure and November restructuring of the debt cost additional USD 52.3 m to the company.

Despite existing debt problems, UZ continued to attract money from banks to plug its financial hole and shortage of rolling stock. For example, in December 2010, South Railway alone raised approximately UAH 469 m from Ukrainian banks and USD 261 m from the Export-Import Bank of Korea and obtained letter of credit opened at amount of USD 46 m.[xxiv] Besides, UZ started public offering of bonds and by August 10, 2010 it raised approximately UAH 0.79 bn with 24% p.a. coupon rate.[xxv] Thus, UZ accumulated large credit resources earmarked for investments.

The UZ has ambitious investment plans. In March 2010, the Investment Committee of the UZ was created entitled to conduct costs and benefits analysis of investment projects and to elaborate short-, medium- and long-term investment plans.[xxvi] Later, capital investments plan for 2010-2014 was presented envisaging UAH 78 bn investment expenditures.

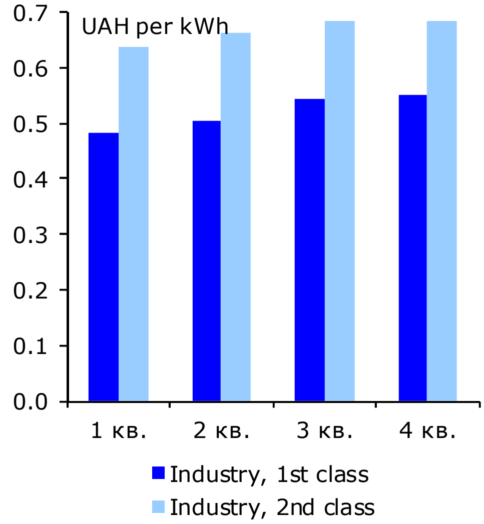
Still, risk remains that borrowed funds would be spent on debt repayment rather than used for modernisation of railways.

In 2010, credits repayment in the roads sector should have been UAH 6.6 bn, including UAH 6.2 bn of payments for sovereign guaranteed credits. Thus, main efforts of Ukravtodor (the State Road Service) were directed towards fundraising. In November, the EBRD provided EUR 450 m loan to Ukravtodor to improve roads near Kyiv. The EBRD financing is followed by a similar-sized loan from the European Investment Bank and by EUR 170 m pledged by Ukrainian government. These funds are necessary to maintain and develop the road system in Ukraine. Again, the risk of their inefficient use is high given Ukravtodor's debt burden and previous credit record.

Reconstruction of airports also required borrowings. In 2010, the state enterprise Boryspil International Airport raised UAH 0.5 bn through public offering of bonds.

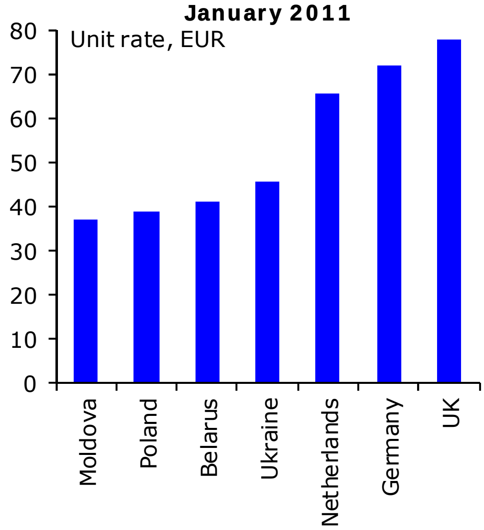
Acknowledging difficulties of transport sector incumbents in infrastructure development, the government directed substantial amounts of public funds towards infrastructure. In particular, in 2010 it earmarked UAH 4.4 bn for road construction and renovation, and UAH 2.7 bn for airports and almost fully financed them (as of December 1, 2010). Those efforts are evoked mainly by preparations for the 2012 UEFA European Football Championship and, therefore, they ensure only minimum level of necessary infrastructure extension.[xxvii] To facilitate renovation and development of infrastructure, sector reforms should be intensified.

Electricity tariffs for industrial consumers in 2010



Source: NERC

Route charges for flights, January 2011



Source: EUROCONTROL

Competition. In July 2010, the Law on Public Private Partnership (PPP) was adopted.[xxviii] This law established general principles of the PPP and defined the scheme of projects preparation and implementation. However, many procedural issues remained outside the law. Moreover, the Ukrainian legislation covered a great part of issues related to PPP a long time ago. Thus, although the adoption of the law is a positive development it is unlikely to boost private participation in the infrastructure projects given unfavourable business environment and absent rule of law.

Two airports were offered for concession in 2010. In March, Scorzonera became concessionaire of Ivano-Frankivsk airport for 30 years, and in December local authorities agreed to grant Vinnitsa airport in concession for 25 years. The concessionaires are obliged to rehabilitate infrastructure and improve passenger hosting. Those developments are the evidence of Ukrainian airports' prospects, though the latter can be fully revealed only if the state refrains from temptation to intervene.

In 2010, the Antimonopoly Committee of Ukraine (AMC) often considered cases in transport natural monopolies, where, according to the law, independent regulator should be created. Meanwhile, the AMC stopped practices of setting higher monopolistic price (airports[xxix]) and of price discrimination (in ports and railways[xxx]) as well as enhanced competition in potentially competitive segments (ports and airports[xxxi]). The AMC asked the MTCU to elaborate methodology of fair tariffs calculation and procedure of access to potentially competitive segments (handling cargo and passengers services) in transport subsectors. Thus, the MTCU fulfils functions of the sector regulator, though it is not independent as it governs state-owned corporate rights in mentioned transport subsectors. Due to lack of competition Ukraine risks fixing its lagging behind positions in infrastructure and economic development.

On the threshold of Common Aviation Area (CAA) with the EU, Ukrainian air carriers consolidate their efforts to compete with European companies. In October, the AMC allowed an alliance between Aerosvit, Donbasaero and Dniproavia[xxxii] for one year. However, companies agreed to set fair tariffs, grant access to Dnipropetrovsk airport, and increase quota of the lowest tariffs from 5 to 20%. As competition for global air space intensifies and the AMC monitors the situation, only positive effects are expected from this alliance. However, if CAA with the EU does not take place in the close future, monopolization of domestic market will harm consumers.

State sector policy. In October 2010, the Transport Strategy for Ukraine until 2020 was adopted by the Cabinet of Ministers.[xxxiii] The Strategy defines main development goals for transport sector as a whole and for separate sub-sectors. Due to its declarative character, the Strategy bears risk of remaining only a "piece of paper" instead of becoming a roadmap to real reforms. Nevertheless, the EU agreed to provide EUR 65 m to Ukraine for implementation of this Strategy,[xxxiv] providing financial stimulus for reforms.

In June, the Ministry adopted Measures aimed at improvement of regulation of road transportation[xxxv]. In particular, they foresee better governance and regulation from the side of the road transport authorities to ensure level playing field on the market. They should also help solve problems of safety, illegal activities, and poor quality of services. However, those Measures can be effective if they are followed by corresponding regulations. E.g., the Ministry toughened qualification requirements for transport companies, in particular to qualification and health of drivers, technical equipment of vehicle[xxxvi], what is expected to contribute to better quality and safety of transport services.

In December 2010, the President reorganized the Ministry of Transport and Communications into the Ministry of Infrastructure[xxxvii]. Each transport subsector and communications now is under responsibility of separated governmental services, coordinated by the new Ministry. Sphere of tourism and preparation for the EURO-2012

Main credits in transport sector

Year	*Borrower*	*Creditor*	*Credit amount*
2007	Ukrzaliznytsia	Barclays Capital Bank	USD 550 m
2007	Ukravtodor	EIB	EUR 200 m
2007	Illichivsk Sea Commercial Port	EBRD	EUR 26 m
2009	Ukravtodor	Ukreximbank	UAH 2100 m + UAH 1920 m (promissory notes)
2009	Ukravtodor	Credit Suisse Investment Bank	USD 465 m
2009	Ukravtodor	World Bank	USD 400 m
2009	Ukrzaliznytsia	EBRD	USD 62.5 m
2009	Odessa Terminal Holdco Ltd	EBRD	USD 37 m
2009	Euroterminal LLC	EBRD	USD 27 m
2010	Ukravtodor	EBRD, EIB	EUR 900 m
2010	Ukrzaliznytsia	Export-Import Bank of Korea	USD 261 m

Sources: EBRD, EIB, mass media

Discounts for handling transit cargo in selected sea ports in 2010, %

	Illichivsk	Odesa	Yuzhnyy
Grain	30		
Pig iron	30	30	30
Ferrous metals	30	30	30
Sulfur (in bulk)	40		
Coal (in bulk)			25
Iron ore			25

Source: MTCU

are new competence fields of the Ministry too. Thus, the Ministry is granted with powers in additional spheres, however, this will hardly help it to better articulate state policy and reform infrastructure since institutional conditions of the sectors remain the same.

Telecommunications. Towards European regulation and mature market

Market access. The National Commission for Communications Regulation (NCCR) has persistently strived for regulatory improvements respecting interconnection and access to telephone channels. In particular, in February 2010, it set recommendatory interconnection fees between all mobile and fixed telecom operators that dominate their market segments[xxxviii]. Yet in June the AMC determined eight major telecom operators as monopolists within their networks[xxxix] and in July those fees became mandatory for them[xl]. However, the allowed tariff corridor became subject to disputes between operators, and the regulator decided to eliminate it. In November, the NCCR adopted draft decision setting 0.25 UAH/min for access to fixed-line networks, and 0.36 UAH/min for access to mobile networks[xli]. Moreover, at the end of the year the Commission was granted the power to determine telecom operators with significant market power (SMP)[xlii] and to set fees for traffic transmission (transit and termination)[xliii]. The fees for all other operators cannot be lower than fees for operators with SMP. As a result, it is expected that dominant companies will not be able to abuse their monopolistic power anymore and mutual access will be fairly regulated by cost-covering fees.

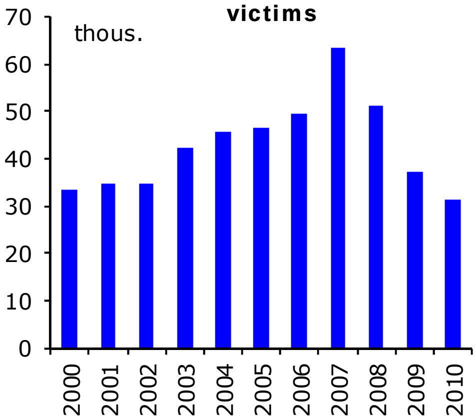
Also, in December 2010 powers of the NCCR were expanded to setting the tariffs for use of telephone channels, 90% of which belong to the state incumbent Ukrtelecom[xliv]. As a result, this new legal provision, Order of access, adopted last year[xlv], should ensure fair access for all telecom companies to channel network and development of alternative fixed-line operators.

In 2010, the NCCR continued its work on conversion of frequencies that can be used for 3G (IMT-2000 (UMTS)) services provision but currently occupied by the Ministry of Defense. In July, the regulator with the Ministry and other bodies created working group on elaboration of plan for conversion of frequencies in band 2 GHz[xlvi]. The Ministry of Defense estimated conversion costs at the amount of UAH 2.5 bn and wanted conversion to be done at the expense of market operators. According to its plan, conversion foresees 3 stages, with the first taking 8 months and costing approximately UAH 850 m[xlvii]. The regulator insisted on compensation of only these costs by claimants for 3G license. The plan was expected to be adopted at the beginning of 2011 so that licenses could be granted as soon as possible.

New licensing rules for many telecommunications services were introduced in 2010. In January, new licensing conditions for the fixed-line services suppliers[xlviii] became effective. Also, in July 2010 the NCCR adopted new licensing conditions for fixed-line services supply through wireless technology[xlix]. Eventually, the CMU followed these decisions and updated its regulation of licenses fees[l], set in 2004. Now, license fees are equal for all operators and do not depend on technology used. In general, those regulations can be positively assessed as new conditions that imply principle of technology neutrality advocated by International Telecommunications Union[li]. However, license for international telephony channels rental became 27 times more expensive and IP-telephony providers suffered since they enjoyed privileged regime before[lii]. So, regulation of the NCCR and CMU should be more predictable and foresee transition periods for parties involved.

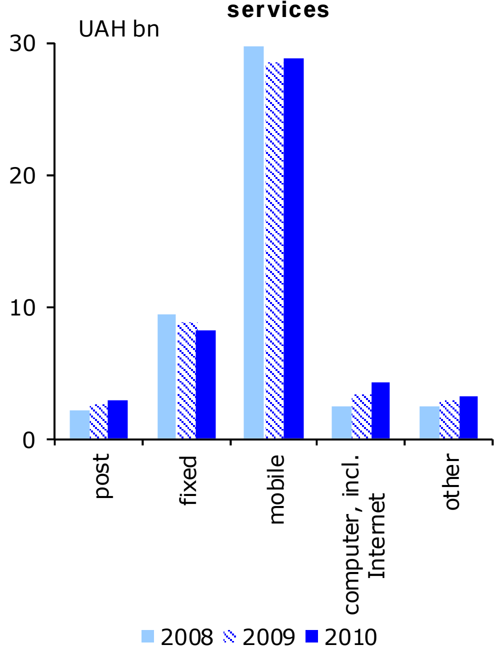
Licensing for post services were eliminated in autumn 2010[liii] and this decision sets free entry in this segment of communications market which allows more liberalization of the market.

Number of road accidents with victims



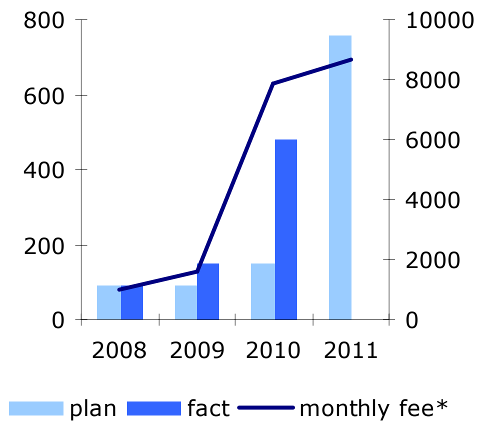
Source: State Road Incspectio

Revenues from communication services



Source: Derzhkomstat

Budget receipts from fees for frequency use



Source: Treasury reports; Ukrainian legislation
Note: * only for cell communications

Consumers protection. During the year the NCCR actively worked on consumer rights issues. In April, the NCCR has introduced regulations "On quality of service in telecommunications",[liv] which set quality parameters[lv] and require the public presentation from telecom operators. The first presentation was scheduled to take place in January 2011. This regulation complies with the EU acquis and will contribute to transparency in operators' activities quality of services.

In July, the Verkhovna Rada amended the Law of Ukraine "On telecommunications" and, therefore, allowed mobile subscribers to port mobile numbers from one service provider to another starting January 28, 2011[lvi]. The NCCR defined that ported mobile numbers will be administered by non-governmental organization chosen by the regulator[lvii].

Besides, the Commission has elaborated jointly with the AMC, other state bodies, and market operators new rules of telecom services provision. The Draft Rules were adopted[lviii] to protect consumer's right to get full and true information about services, their provision conditions and related changes, real prices and quality. They also increase responsibility of all parties for breach of rules. Thus, the regulator proved it was able to balance interests of all involved sector agents.

Tariffs and fees. State tariff policy regarding universal communications services remained unchanged. However, in April, the Cabinet of Ministers increased fees for usage of frequency spectrum reserved for cell communications five times [lix]. Moreover, all frequencies became 10% more expensive in the new Tax Code[lx]. The decision was motivated by fiscal considerations. However, a net impact on fiscal revenues is ambiguous, as higher costs of telecommunications would result in lower profits and thus lesser enterprise profit tax collections unless these costs are completely passed to consumers. Moreover, a lot of small companies will simply leave the market.

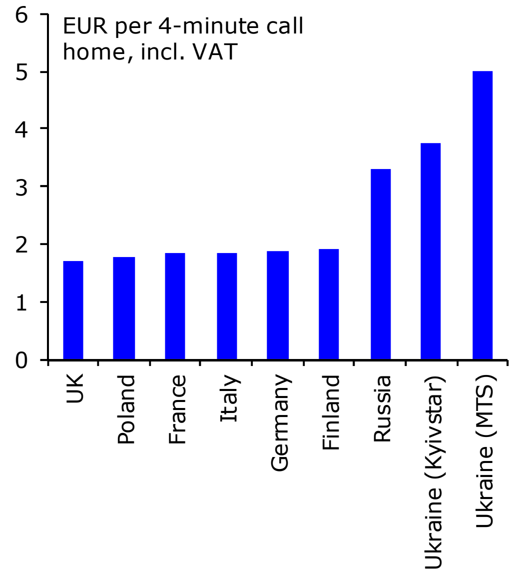
In July, the AMC started investigation of tariffs for roaming provided by Ukrainian mobile operators. In particular, it revealed that their values are substantially higher than in other countries[lxi]. Eventually, it required 7 mobile operators to reduce tariffs for roaming. As a result, MTS and Kyivstar have already promised to make them twice less expensive for CIS countries[lxii].

To crown it all, it can be noted that independent regulators act in more apprehensible manner than the government pursuing fiscal interests.

Monopolies on the market. In 2010, telecom market developments were to a great extent explained by behavior of the largest monopolies. So, in 2010, financial performance of Ukrtelecom slightly improved. First, the Ministry as a manager of state-owned corporate rights charged the company with quarterly reports on financial results[lxiii]. Second, in May, privatization of this company was announced, so efforts to improve performance were intensified. Thus, the company repaid USD 55.6 m of USD 500 m debt to Credit Suisse First, Deutsche bank, and Standard bank[lxiv]. However, liabilities of the company were still significant. And it had accumulated more by the end of 2010[lxv]. In addition, Ukrtelecom postponed tax and labour payments[lxvi], dismissed personnel. At the same time, it managed to increase revenues from broadband Internet services. All those steps allowed the company to show better results, which may appear to be short-term and signalize only preparations for announced privatization.

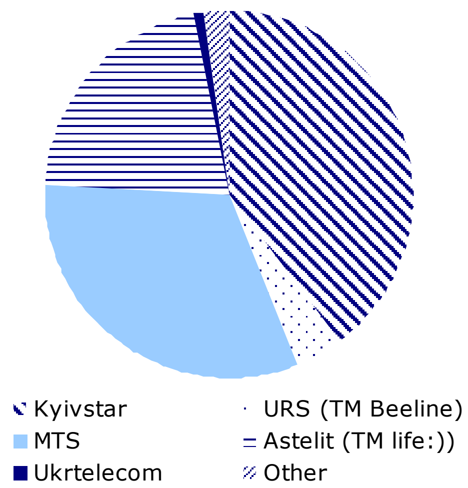
In March 2010, the AMC approved the merger of Ukrainian assets of Telenor ASA and Altimo Holdings & Investment Ltd, i.e. large telecom operators URS and Golden Telecom (TM Beeline) and Kyivstar. Existing legislation does not provide limitations on obtaining some or even all licenses and radio frequencies by one participant[lxvii]. Thus, the united company concentrated significant resources[lxviii] and,

Roaming charges



Source: Europe's Information Society, AMCU, Federal Antimonopoly Service of Russia
Note: Data for Ukraine and Russia is of autumn 2010, for the EU - summer 2010

Mobile market structure, by share in subscribers number*



Source: proIT
Note: * July 2010

therefore, market power. And even after revision of the AMC's decision[lxix], the case was closed and merger allowed[lxx].

So, given slower revenues increase in the sector, telecom operators consolidate their assets to compete in tougher conditions.

Utilities: Reforms scheduled

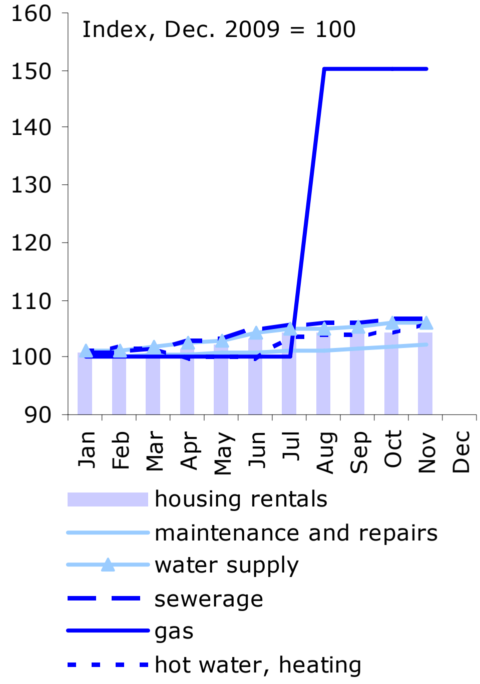
In 2010, there were several important changes in organization and regulation of the utility sector.

The most important development was an establishment of an independent regulator for public utilities[lxxi] – the National Regulatory Commission for Public Utility Markets of Ukraine. Creation of the Commission is envisaged by the Law of Ukraine.[lxxii] The Commission aims to balance interests of stakeholders on the market by setting tariffs for heating, water supply and wastewater treatment services, licensing and controlling compliance with licenses conditions. The Commission should have begun its operations starting January 2011. Until full operation of the commission the tariffs will be set by the National Electricity Regulatory Commission or left at an existing level. Thus, tariff-setting function is taken from the local authorities and transferred to the national level, which, in principle, diminishes political interference into tariff setting. It is also expected that cost coverage of utility tariffs will improve, which in turn will improve financial state of the enterprises of the industry.

At the same time, the Law on the Commission has several important drawbacks. First, there is not enough human and financial capacity envisaged to perform appropriate tariff assessment and following tariff setting.[lxxiii] Second, there is no procedure to assess the envisaged tariffs. Thus, at least at the first stage, the Commission will not check economic sense of the tariffs. Third, the regulation framework does not foresee instruments to stimulate utility companies to save energy, increase investments, and cut costs. Thus, there is a good chance that the instrument of independent regulation will be highly underutilized.

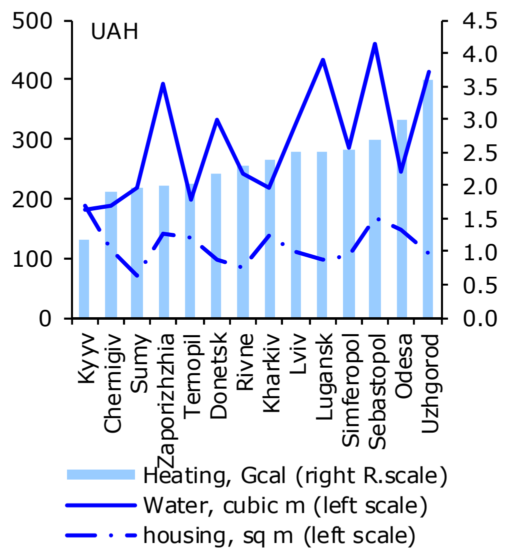
From August 1, 2010, gas tariffs for households and gas prices for district heating enterprises were increased by 50%. As a result, tariffs for heating services most probably are likely to increase, which has already happened in several regions of Ukraine. Together with the increase in gas prices for population, the tariffs and an anticipation of rises of other utility tariffs, the CMU changed the eligibility conditions for a utility subsidy for households. Therefore, the most vulnerable population was to become protected from the increase in utility tariffs.

Price indices for utilites in 2010



Source: Derzhkomstat

Tariffs for housdeholds as of Jan 1,



Source: Derzhkomstat

External sector: Surplus of financial account compensated for current account deficit

According to the NBU current account deficit widened to USD 3.0 bn (2.2% of GDP) in 2010 as compared to deficit at USD 1.8 bn (1.5% of GDP) in 2009 due to growing trade deficit. The deficit was covered by the financial account surplus at USD 7.9 bn.

Current account. In 2010 international trade was gradually recovering. The current account deficit was explained by sharp imports in increase in the second half of 2010, which outpaced exports growth rates. Imports growth was stimulated by higher investment and consumption demand. At the same time, the external demand for Ukrainian products remained weak, though partially recovering from the crisis. Resulting merchandise trade deficit almost doubled to USD 8.4 bn. It was partially compensated by surplus in trade of services and positive current transfers. Overall, the trade deficit doubled to USD 4.0 bn.

Financial account. Financial and capital account surplus reached USD 7.9 bn. The surplus was ensured by positive net inflow of FDI and portfolio investments. Besides, net foreign borrowings were positive partially due to issue of state the Eurobonds by the Government. At the same time, the financial and capital account surplus was suppressed by large cash purchases of foreign currency.

Merchandise trade: Domestic demand resulted in imports recovery

According to the Derzhkomstat, in 2010 merchandise trade deficit increased by 62% to USD 8.4 bn, being lower than before the crisis.

Merchandise export increased by 29.6% in dollar terms in 2010. The growth was registered across almost all product groups. The exports of the vehicles more than doubled partially due to increase in demand for locomotives. Besides, the exports of products in the Group V 'Mineral products' grew by 72.6%, which was attributed to higher sales of ore.

Metal exports somewhat revived after the crisis stimulated by higher world demand and price increase. Exports of the Group XV 'Non-precious metals' increased by 35.2% in dollar terms. These products retained the highest share in the total exports (33.7%). However, this share remained about a fifth lower than before the crisis, indicating important reshuffling in the structure of exports.

Exports of vegetable products were among few export groups that contracted. Overall, their sales abroad declined by 21.0% mostly due to grain export restrictions (see *Agricultural policy*).

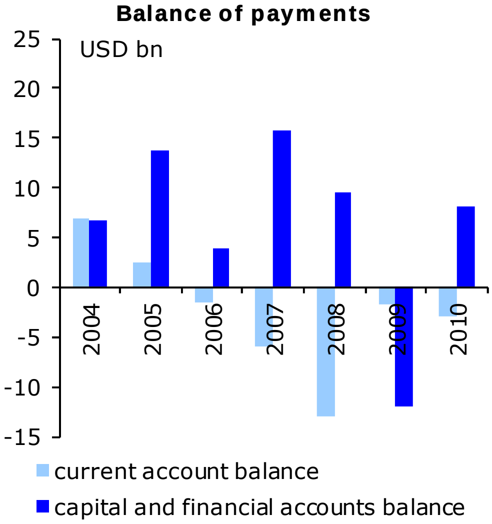
Merchandise imports increased by 33.7% in dollar terms, with all product groups except for Group I 'Live animals and animal product' demonstrating growth. The largest contributors to imports increase were mineral products with 34.8% share in total imports and 34.6% growth rate. Sharp increase in exports of this group is explained by higher domestic demand for oil and gas as well as higher prices for these products.

Domestic demand recovery strengthened in the second half of the year (see *GDP*) also stimulating imports increase. In particular, imports of Group XVII 'Vehicles, aircraft, and associated transport equipment' increased by 69.3%.

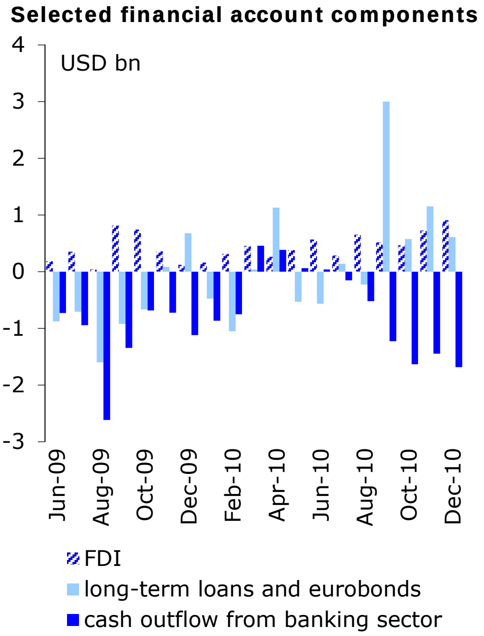
CIS countries have the largest share in trade with Ukraine (36.5% – export, 44% - import). In 2010 merchandise trade with CIS countries increased largely due to the intensification of trade with Russia and Belarus. Certain Government's economic agreements with Russia boosted trade between two partners. Among the discussed issues were increase of export quotas of sugar-beet sugar to Russia to 300 thousand tons, join projects in aviation sector, inter banks agreements to support export finance, duty free import of Ukrainian pipes to Russia, renewal of Ukrainian export of milk and meat products. Exports and imports grew by 61.5% and 74.7%, respectively, in nominal terms. Remarkably trade with Belarus (which formed Customs Union with Russia and Kazakhstan) also increased: by 50.9% in exports and 51.7% in imports, although this country has a low share in total trade volumes with Ukraine. In 2010, Russia became the largest trading partner of Ukraine, surpassing the EU-27 customs territory. In particular, the shares of exports to Russia and to the EU-27 constituted 26.1% and 25.3%, respectively, while the shares of imports were 36.5% and 31.5%, respectively. Total merchandise exports and imports volumes to CIS countries made up 36.5% and 44%, respectively.

The EU-27, the second largest Ukraine's trading partner, kept its share in total export volumes almost on the 2009 level – 24.9%. Among the EU-27, Italy, Poland and Germany are the primary export destination countries for Ukrainian products. Exports to those countries increased by 99.4%, 47.5% and 20%, respectively. The leading importers were Germany with 7.5% share (19.5% growth), and Poland with 4.6% share (28.5% growth) in total merchandise imports.

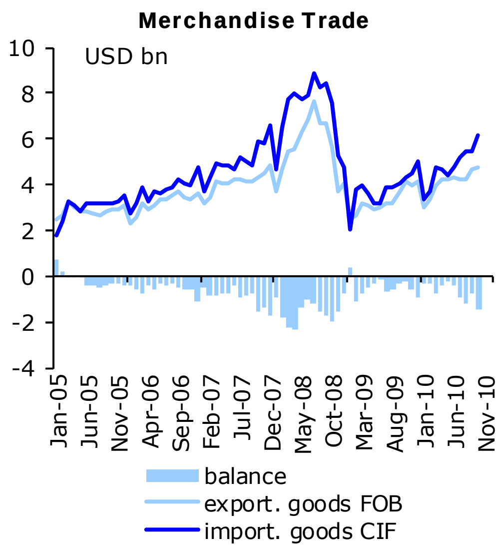
Ukraine's merchandise export to Asian countries constitutes 26.7% of export volumes and increased by 13.1%. Import from these countries grew by 53.6% and constituted 16.5% of all imports. In Asia Ukraine traded mainly with India and China.



Source: NBU



Source: NBU preliminary estimates



Source: Derzhkomstat

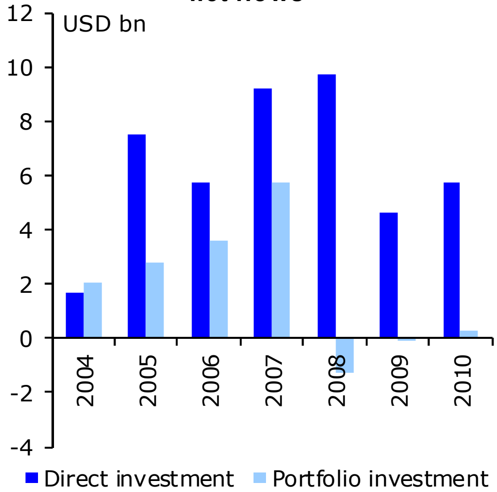
Overall, Ukraine's foreign trade recovered in 2010. Domestic demand drove imports growth, and export revived amid strong economic performance of developing countries and moderate recovery of advanced economies. Among trade constraints export quotas and barriers were the most pronounced significantly impeding grain exports.

Migration: Ukraine signed Visa Action Plan with the EU

Regulations. The most important achievement of the year is the Visa Action Plan, received from the EU as a part of visa dialogue between parties. The Action Plan foresees technical conditions to be fulfilled by Ukraine in order to progress with visa liberalization issues for short-term travelers. Visa liberalization is pursued to reach visa free movement for Ukrainian citizens to the EU. The plan provides for introduction of biometric passports in Ukraine, enhancement of border and migration control, changes in asylum policy, reforms in public security and order, border management, and counterfeit of illegal immigration. All goals are grouped in two phases and the progress is to be examined by the EU Commission and Council. The first report is scheduled for the middle of 2011. Ukraine's diligence to execute the plan will require significant institutional and regulatory changes. The EU doesn't set any concrete time-frames for achieving those goals. The proper execution of the plan is of significant importance for deepening visas and migration issues between EU and Ukraine and is to ensure visa free movement for short-term visits of Ukrainian citizens to the EU.

Migration flows. In 2010, official outflows of migrants reduced by 24.6% to 14.7 thousand persons. Tougher regulations on external labour markets after the crisis and lower labour demand are main reasons for this downturn. The number of arrivals decreased much lesser (by 6.4%), and in western regions this number even grew. This trend could be explained by the return of labour migrants from the EU where they faced tougher labour market conditions. Net balance of migration remained positive, and increased by 20% to 16.1 thousand.

Foreign direct and portfolio investment net flows



Note: E - estimate, F - forecast
Source: NBU, IER calculations

Wages and income: Real disposable income exceeded 2008 level

Improved financial state of enterprises and higher fiscal revenues against the background of decelerated inflation resulted in restoration of real disposable income in 2010 above the levels of 2008.[lxxiv] According to the Derzhkomstat, real disposable income grew by 16.2% in 2010 compared to 8.5% decline in the 2009. The income from all components increased.

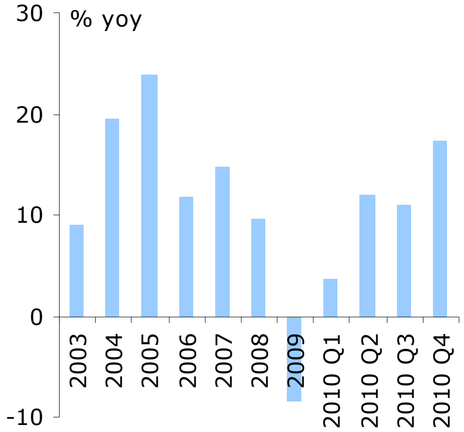
Real wage income grew by 14.9% in 2010 due to increase in wages and decline in unemployment (see *Labour Market*).

In 2010 average wage increased by 20.0% in nominal terms and 10.2% in real terms.[lxxv] It reached UAH 2629 in December. Improved financial situation of companies (see *Financial State of Enterprises*) and higher productivity determined upward trend in wages. Administrative increases in minimum wage also remained among important drivers of average wage growth (see *Social Policy*).

Nominal wages increased in all sectors of the economy in 2010. The highest wage growth was registered in industrial sectors (by 24.6%). Civil servants' wage increased at the lowest rate (by 7.3%) likely due to continued tight wage policy in public administration. The wage disparities remained. In 2010, financial sector paid the highest average wage at UAH 4602, while the lowest average wage (UAH 1430) was traditionally paid in agriculture.

Income from social assistance and current transfers increased by 16.2% in nominal terms and 6.2% in real terms. The growth was supported by increase in social standards (see *Social Policy*). Real income from entrepreneurship and subsidiary farming increased by 13.5%.

Real disposable household incomes



Source: Derzhkomstat

Lower debt burden was among contributors to the disposable income growth. In particular, income from dividends and interests on deposits increased by 50.3% in real terms 2010. At the same time, households' spending on loan interest payment declined by 27.0% in real terms due to lower credits outstanding.

In general, welfare improved in 2010 thanks to economic recovery. Companies paid higher wages, unemployment subsided, while the Government ensured timely pension payments (see *Pension policy*). Households' debt burden also reduced as stock of outstanding credits to households lowered.

Labour market: ILO unemployment rate remained above pre-crisis level

Unemployment rate (ILO). The economic recovery in 2010 resulted in decline in unemployment rate defined according to the International Labour Organisation (ILO) methodology. Still, it remained below the pre-crisis level.

According to the Derzhkomstat, in 2010 unemployment rate (ILO methodology) was at 8.1% of economically active population between 15 and 70 years old as compared to 8.8 % in 2009.

Faster decline in unemployment rate was registered for male who suffered more from dismissals in 2009. This is explained by larger male employment in volatile sectors that sharply dropped their production in 2009 and then partially recovered in 2010. Still the unemployment rate for male remained higher than for female (9.3% and 6.8%, respectively), and the spread between them remained higher than before the crisis.

Unemployment rate in urban area declined by 1.0 p.p. to 8.6%, while rural unemployment merely reduced by 0.1 p.p. to 7.1%. It is explained by recovery in industry and financial services, i.e. sectors prevailing in urban areas, and decline in agricultural output in 2010.

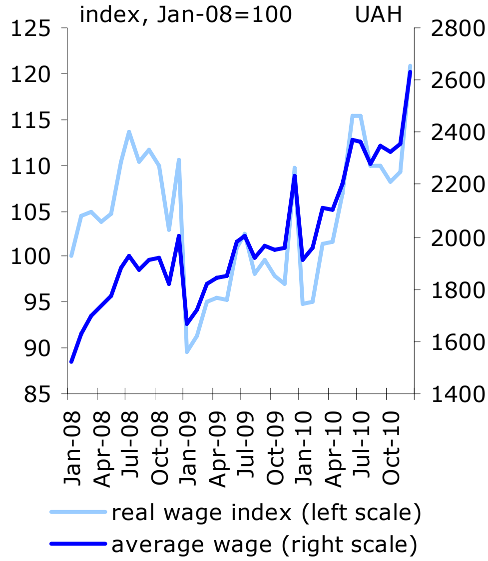
Registered unemployment rate. The number of unemployed registered in the State Employment Office was lower than before the crisis. The registered unemployment rate declined from 1.9% of working able individuals in January to a minimum of 1.4% in summer and then picked to 2.0% in December.[lxxvi] For comparison, it was 2.3% in pre-crisis December 2007. Low registered unemployment rate is likely attributed to amendments to the legislation made in the end of 2008, toughening registration requirements.[lxxvii]

The average placement ratio was higher in 2010 than in 2007, signalling about some improvement in active labour market measures. Nevertheless, this ratio declined rapidly in the end of the year against the background of drop in number of open vacancies. The number of unemployed per one vacancy increased to 88 in December 2010, the level of May 2009 against the background of simultaneous increase in unemployment and reduction of vacancies. The number of vacancies declined to 63.9 thous., being lower than during the crisis. This might signal about possible weakening of the labour market as well as uncertainty of employers concerning future development.

General Agreement: In November 2010, the Cabinet of Ministers, representatives of trade unions and employers signed the General Agreement for 2010-2012. This document records agreement between social partners and regulates key aspects of social and labour relations. This concerns employment guarantee, wages, social standards, work safety, etc. Thus, the Agreement reflects consensus of parties on the future development.

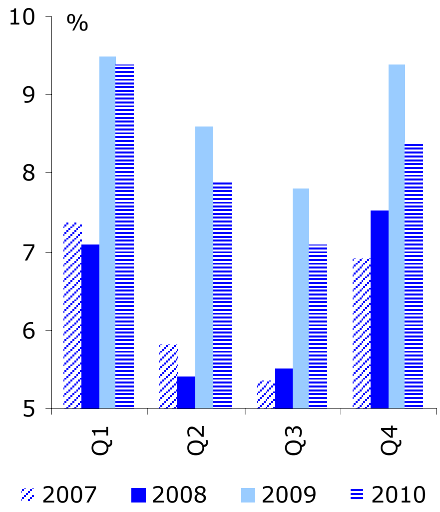
Stipulated in the General Agreement major obligations of social partners are rather declarative and populistic. In particular, parties agreed to ensure the average nominal wage increase by 17.8% in 2010, more than 15% in 2011 and more than 16% in 2012. Employers' representatives promised to set base wage in the tariff scale at the level exceeding minimum wage.[lxxviii] Minimum wage should approach 45% of average wage in economy.[lxxix] At the same

Average wage



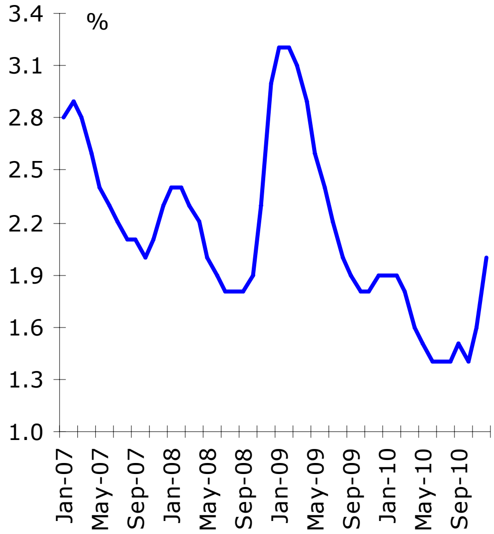
Source: Derzhkomstat

Unemployment rate (ILO)



Source: Derzhkomstat

Registered unemployment rate



Source: Derzhkomstat

time, the Government promised to refund VAT in time and in full, as refund arrears is an essential problem for export-oriented companies.

Fiscal Policy: Fiscal reforms moved forward

Budget process 2010. Ukraine entered the fiscal year of 2010 without approved Budget Law for the first time since 1997 due to lack of political consensus between the President, the Government and the Verkhovna Rada. As a result, one of the first tasks faced by new Government appointed after the Presidential election was an elaboration of the State Budget Law. The document was approved in the end of April with a deficit at UAH 57.7 bn[lxxx] (or 5.3% of GDP).[lxxxi] The deficit was mainly to be financed at the expense of borrowings (see *State Debt*), while privatization receipts were planned at UAH 10.0 bn (see *Privatisation*). The central fiscal revenues and expenditures without credits were planned at UAH 267 bn and UAH 324 bn (24.7% and 29.9% of GDP, respectively). The Budget Law envisaged the issue of the VAT-bonds for reimbursing VAT arrears, which have been proven as of May 1, 2010 (see *State Debt*).[1]

Even though fiscal parameters were approved on the realistic macroeconomic forecast, planned central fiscal revenues were optimistic. In particular, the Government overestimated the impact of the improved VAT administration envisaged in the amendments to the tax legislation, which were made simultaneously with the budget approval.[lxxxii] Besides, the fiscal plan did not elaborate introduced by that legislation zero VAT rate for gas imports.

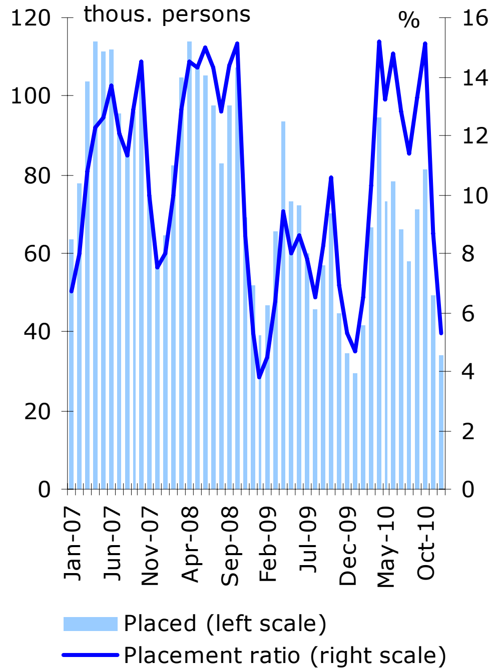
As a result, on July 8 the Government sequestered the budget reducing planned revenues by 5.0% to UAH 253 bn mainly due to lower VAT collections.[lxxxiii] Simultaneously, the target of central fiscal expenditures was decreased by 5.3% to UAH 306 bn. Near 80% reduction concerned spending from the special fund of the budget. The planned central fiscal transfer to the Pension Fund was reduced by UAH 3.0 bn due to changes in the pension legislation. As a result, the target of central fiscal deficit was reduced by UAH 3.7 bn to 4.99% of GDP.

Execution of the Budget 2010. Fiscal pressure remained high during entire year. During entire year tax revenues remained lower than planned. Fiscal revenues in 2010 were under-executed by 4.0% of the amended plan due to lower than planned tax revenues. They grew only by 6.7% as compared to 2009, which is partially attributed to the accounting of refunds reimbursed by VAT-bonds in net VAT collections. Cash VAT refunds declined by 30% in 2010, even though nominal exports increased (see *Balance of Payment*). This was mainly attributed to changed tax administration with more thorough checks to avoid fraudulent refunds.[lxxxiv] Net VAT collections were under-executed by 4.8% due to over-estimated revenues from the VAT paid on imports. The latter could be partially attributed to the imports of oil and petroleum products without VAT payment.

Revenues from excise tax were by 7.1% lower than target due to under-execution of the collection of the tax from domestically produced goods. It is likely to be explained by the overestimation of the elasticity of increase in tax rate on the revenues. At the same time, the execution of the EPT revenues improved by the end of the year against the background of better financial state of enterprises. For the year they were only by 0.4% lower than plan. Revenues from taxes on international trade were over-executed by 1.1% due to recovery of imports. Overall, tax revenues were by 4.3% lower than plan, growing by 12.1% as compared to 2009.

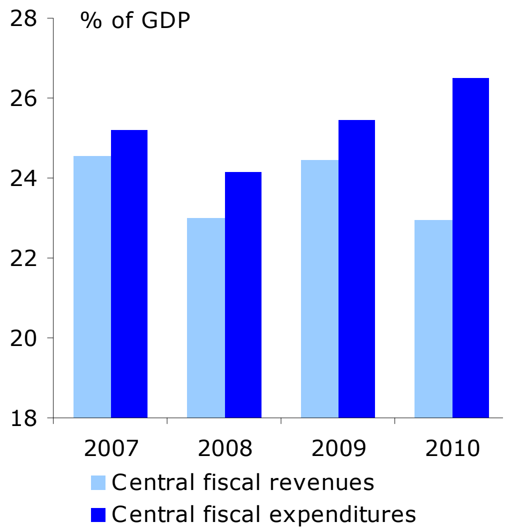
Non-tax revenues were under-executed by 2.5% of the target. In particular, dividends paid by state-owned companies to central coffers and own revenues of budget entities were lower than planned. Besides, the revenues from sale of military surplus were

Placement indicators



Source: Derzhkomstat

Central fiscal revenues and expenditures



Source: the State Treasury reports

[1] VAT-bonds were issued in August only at UAH 16.4 bn for reimbursing VAT refunds arrears proven as of January 1, 2010.

executed only at 8.0% of the target.[lxxxv] At the same time, the NBU has transferred to the budget UAH 15.5 bn, which was by 55.5% higher than planned amount. Therefore, the NBU has again fuelled the budget with additional funds helping the Government to finance its liabilities.

Central fiscal expenditures were under-executed by 6.9% of plan regardless high borrowings, which were not all used by the end of the year (see *State Debt*). Execution rate of current central fiscal expenditures was at 95.8% of target. All items were under-executed except for payment of interest on debt, which reached 5.5% of total central fiscal expenditures. At the same time, capital spending were financed only at 68.3% of amended plan, even though they doubled as compared to previous year.

By functional spending classification, none of the functions was fully financed. The lowest execution rate was for environment protection, which was financed only at 37.8% of the plan. Actual expenditures on defence as well as on housing and utility sector were at near 83% of the target. The economic activity items were under-financed at 16.2% of the plan. In particular state support of most sectors was lower than planned with high under-execution of road construction. Traditionally, the highest execution rate was for social protection (at 97.6% of the target). At the same time, intergovernmental transfers appeared to be lower by 4.4% than plan, which was likely to exacerbate the already difficult fiscal situation at local level.

The central fiscal deficit in 2010 was officially reported at UAH 64.4 bn, being by 15.9% lower than amended plan. As a result, the Government met fiscal target defined in the Stand-by Arrangement. The deficit was financed equally by domestic and external borrowing (see *State Debt*), while privatisation receipts remained low (see *Privatisation*). As the Government did not spend all attracted funds in 2010, it started new fiscal year of 2011 with unusually high amount of funds for financing its liabilities.

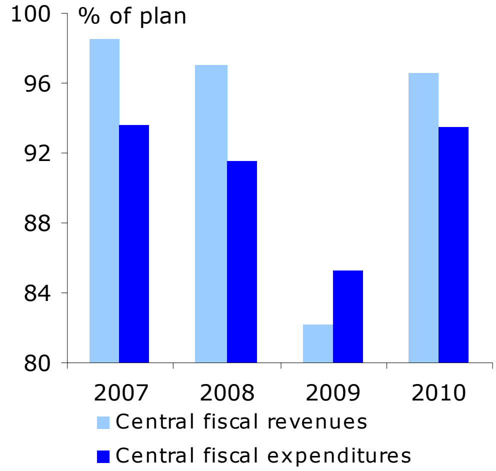
Budget Code: In July 2010, the Parliament approved new version of the Budget Code.[lxxxvi] The document envisaged the introduction of the medium term expenditure framework (MTEF) as well as implementation of the program targeting method of elaboration and execution of central and local budgets. Besides, the coverage of fiscal issues regulated by the Code was enlarged. In particular, the document now includes definition of protected spending items, which previously were defined in each Budget Law.[lxxxvii] Besides, the Budget Code now defines the clear grounds for granting investment subsidies to local budgets from the central coffers. At the same time, as previously, the Code does not define the marginal size of the deficit.

One of the declared goals of the document was to increase fiscal decentralisation through providing local government with higher autonomy and better opportunities to raise own financing. Local governments received additional sources of revenues in the form of part of payment for certain types of licences and certificates, state registration, fraction of duty on water usage, etc. However, in December, the fiscal autonomy of local governments was reduced.[lxxxviii]

Initially the local governments were also granted the right to set additional EPT rate, which was due to local budgets for financing capital outlays. However, as this provision was not reflected in the Tax Code, it was eliminated from the Budget Code in the end of 2010.[lxxxix] As a result, local budgets did not receive significant additional source of financing capital spending.

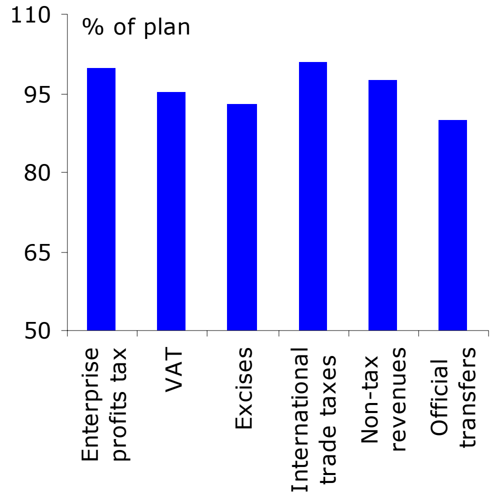
The amendment to the Budget Code made in December 2010 also endangered fiscal position of Kyiv. Starting 2011, 50% of personal income tax (PIT) paid in Kyiv, which is one of the largest sources of local fiscal revenues is to be transferred to central budget.

Execution of central fiscal revenues and expenditures



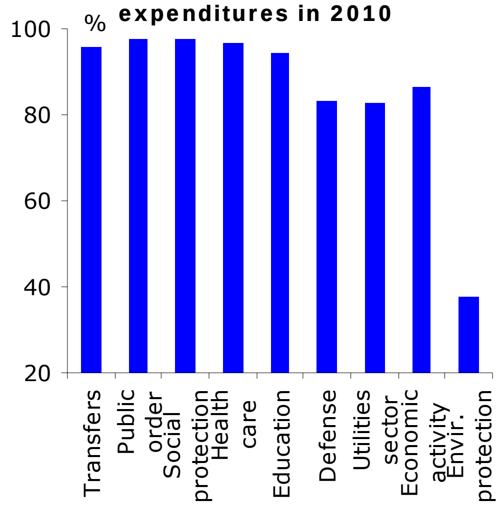
Source: State Treasury reports

Central fiscal revenues in 2010



Source: State Treasury reports

Execution of central fiscal expenditures in 2010



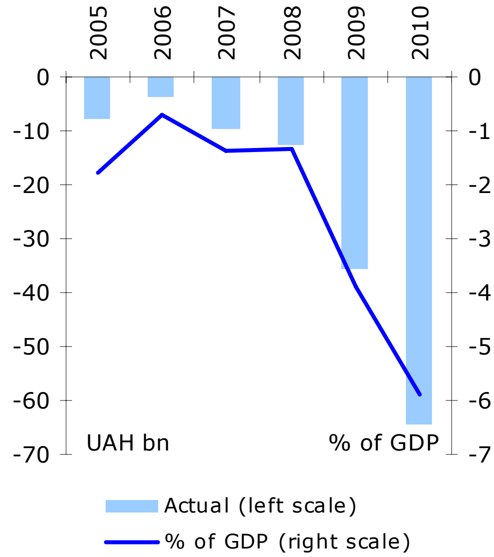
Source: State Treasury

The Budget Code increased the role of the Government in the budget process. In Particular, Budget Resolution is now substituted by the Budget Declaration, which is to be prepared by the Government and its approval by the Parliament is not envisaged. The Cabinet of Ministers has also received more rights in defining investment programs to be financed from the State Budget as well as in the field of borrowing.

Therefore, new version of the Budget Code could be considered as a step forward budget reform, but not a complete reform. The local budgets have received potential for increase in revenues and clearer rules. However, December amendments have again endangered position of local governmental entities.

Approval of the Budget 2011. The State Budget Law for 2011 was approved in December 2011. It is based on the provisions of new Budget Code and Tax Code, which were simultaneously amended. Fiscal parameters are based on the realistic macroeconomic forecast. Central fiscal revenues are planned to reach UAH 281 bn. At the same time, they will decline in relation to GDP due to introduced EPT privileges, zero VAT rate for gas imports and some other changes in tax legislation. However, there is a risk that the Government again overestimated the impact of administrative measures on the limiting the VAT refunds amount. Central fiscal expenditures will increase to UAH 322 bn. The document envisages the increase in capital expenditures against the background of restricted growth of social standards.

Central fiscal balance



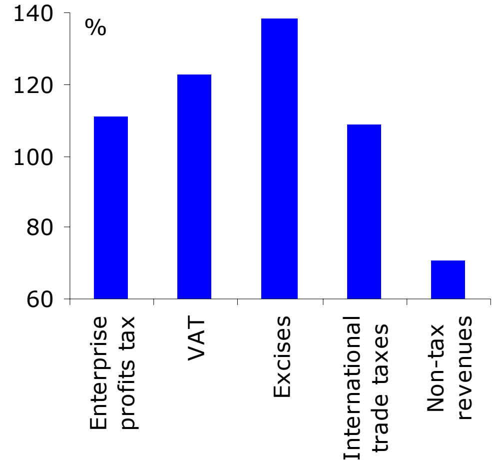
Source: State Treasury Reports

The central fiscal deficit is expected to decline to UAH 38.8 bn or 3.1% of GDP. It will be financed at the expense of domestic and external borrowing, which will remain large. At the same time, the borrowing could appear to be larger in 2011 as the State Budget Law foresees the right of the Cabinet of Ministers to issue domestic state bonds for financing the deficit of the Naftogaz. Additional issue could be placed for the needs of Agrarian Fund. Such policy could endanger the further cooperation between Ukraine and the IMF.

Tax policy: The Tax Code was approved

The approval of the Tax Code was one of the hottest topics for discussion in the second half of 2010. The first draft of the Tax Code was elaborated by the Government rather quickly. It was submitted to the Parliament on June 15 and approved in the first reading two days later. The text of the document combined regulations on all taxes, eliminating their controversial provisions. However, it resulted in opposition of many tax payers as it envisaged increase in competences of tax authorities and *de factor* liquidation of the simplified taxation system (STS) for B2B services providers.[xc] In particular, tax administration has received more powers in conducting off-scheduled inspections. After public hearings conducted in many regions, the document was recalled by the Government on September 7.

Planned central fiscal revenues in 2011 as compared to 2010*



* comparison with ammended planned indicators for 2010
Source: State Treasury reports, State Budget

New version of the Tax Code was submitted to the Parliament on September 21 and was approved in the first and second readings on October 7 and November 18, respectively. The document has somewhat reduced competences of the tax administration, which has still remained large. However, the document still envisaged *de facto* liquidation of the STS, which resulted in strikes of small entrepreneurs and finally in the Presidential veto. The finally approved version of the Tax Code does not contain the chapter on the simplified taxation system. Overall, the Tax Code became effective since 2011, while the chapter on the EPT was enforced starting second quarter of 2011.

According to the approved Tax Code the enterprise profit tax (EPT) rate will decline from 25% in 2010 to 23% in 2011 and then gradually to 16% in 2014. The number of differences between commercial and tax accounting substantially declined, which makes accounting and reporting easier. However, since 2012 companies will have to conduct the third type of reporting on reconciliation of discrepancies between two forms of reporting. The depreciation rules will become closer to the EU norms. However, further improvement are needed. In particular, while there are defined 16 groups of fixed assets, most assets fall under four groups. Even though, the Government remained unchanged STS, the Tax Code stipulated that legal entities working under general taxation system cannot deduct payment to STS taxpayers (except for IT services) from profit subject to EPT. Therefore, legal entities are *de facto* discouraged to work with the STS taxpayers. At the same time, the Tax Code envisages zero EPT rate for small new-starters for five years. Companies of light industry, hotels and restaurants will enjoy 10-year EPT-break. Such privileges do not seem to be substantially economically justified.

The VAT rate will be reduced from 20% to 17% in 2014. Taxpayers with good tax record are promised to receive VAT refunds automatically. The VAT rules for agricultural sector were changed. The PIT rate will become slightly progressive with base rate at 15%, while 17% will be paid on incomes over 10 sizes of minimum wage. At the same time, the Government postponed taxation of deposit interest until 2015.

Several local taxes and duties were eliminated due to their inefficiency. At the same time, property tax is to be introduced in 2012. However, for efficient introduction of this tax the Government has to conduct substantial work in 2011. In particular, clear property registry is to be formed.

The final version of the Tax Code kept provisions on larger competences of tax authorities, which were not counterbalanced with increasing rights of taxpayers. In particular, the tax authorities received more rights in relation to reasons and procedures of inspections.

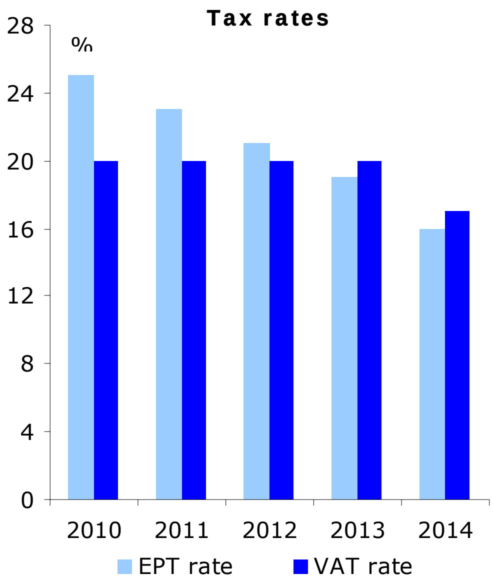
Overall, the approval of the Tax Code is a first step forward tax reform. Most provisions remained similar to old regulations. The Code is mostly fiscal document, which does not suggest additional incentives for economic development. It is likely that it will allow Ukraine to go upwards in the *Doing Business* rating due to declined number of local taxes, lowered tax rates, and reduced number of legislative acts to be dealt with while paying taxes in Ukraine. However, it might increase pressure from the tax authorities, which would negatively impact investment climate.

Social policy: Social standards rapidly increased

Social standards and minimum wage in 2010. A swift increase in social standards and minimum wage was passed by the Parliament in November 2009,[xci] on the eve of presidential election campaign. But the decision was implemented only in May when State Budget Law came in force (see *Fiscal Policy*). The general level of subsistence minimum was raised retroactively to UAH 825 for January. It reached UAH 875 in December. Total increase was 32.1% on average per year. Minimum wage was increased from UAH 869 in January to UAH 922 in December.

Wages in the public sector. The differentiation in public sector wages narrowed in 2010. In May, the Government retroactively increased the first tariff rate in the Unified Tariff Scale (UTS) used for paying wages to public sector employees to UAH 555 from January.[xcii] The rate was then gradually raised to UAH 600 in December. During the year, the level of the first tariff rate in the UTS increased from 63.9% to 64.5% of minimum wage. Overall, minimum wage was paid to employees up to the seventh tariff class (out of 25 tariff classes).

Unified social contribution. In 2010 the Parliament approved long-awaited the Law on Unified Social Contribution (USC), which has become effective since January 2011.[xciii] The USC combines pension insurance contributions and three social insurance contributions. The



Source: Laws of Ukraine, Tax Code

Subsistence minimum, UAH

	2010		2011	
	Jan.	Dec.	Jan.	Dec.
General level	825	875	894	953
In particular:				
For children less than 6 years old	755	799	816	870
For children of 6-18 years old	901	957	977	1042
For working able individuals *	869	922	941	1004
For individuals that lost ability to work**	695	734	750	800

Note: * minimum wage
** minimum pension
Source: the State Budget Law for 2010, the State Budget Law for 2011

Pension Fund is responsible for its administering. The USC rate varies according to 67 classes of occupation risk from 36.76% to 49.70% of wage and is paid by insurer, for instance employer. The contribution of employees is set at 3.6% of gross wage. Individuals working under the simplified system of taxation should pay contribution at least at the level of 34.7% of minimum wage. The contribution base is capped by 15 sizes of minimum wage. The Law does not cause a reduction in payroll tax burden. However, its introduction might result in lower administrative burden on companies, as the number of payments, reports and inspections are expected to decline.

Housing and utility subsidies: In 2010, the Government amended the procedure of providing housing and utility subsidies to households. The decision was aimed at increasing subsidy coverage to counterweight growing housing and utility tariffs. Changes became effective as of August 1, simultaneously with increase in gas tariffs for population. The upper bound for the share of households expenditures on housing and utility services in income, which makes families eligible for the subsidy, was reduced from 20% to 15%. This share declined by 5 p.p. to 10% for households consisting only of pensioners, children under 18 years old and disabled individuals. The procedure for application for the subsidy was facilitated. Such changes increased the number of potential recipients of the subsidy. Between August and November the number of applicants reached 1491 thous. persons being by 2.5 times higher than in the same period of 2009.

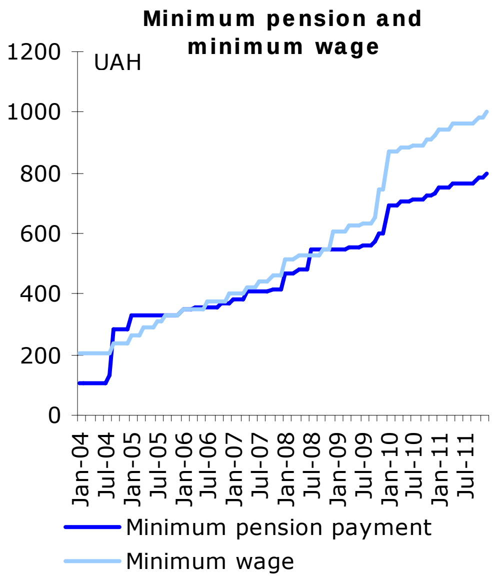
At the same time, the efforts of local social offices were largely directed towards rigorous enforcement of eligibility criteria. Such criteria include the restriction on large purchases made during recent year and obligatory economic activity of working able individuals. As a result of more thorough inspections the number of rejections increased by 18.2 p.p. to 60.5% of applicants for the subsidy. Therefore, better enforcement made it harder to receive subsidies by average applicant.

Social assistance: The guaranteed level of subsistence minimum, which is used for paying social assistance for low-income families, was also rapidly increased in 2010. It increased on average by near 40%. At the same time, the birth grants were not changed. Starting 2010 both types of social assistance will be defined in relation to subsistence minimum level. As a result, they will increase automatically each year in line with the growth of subsistence minimum.

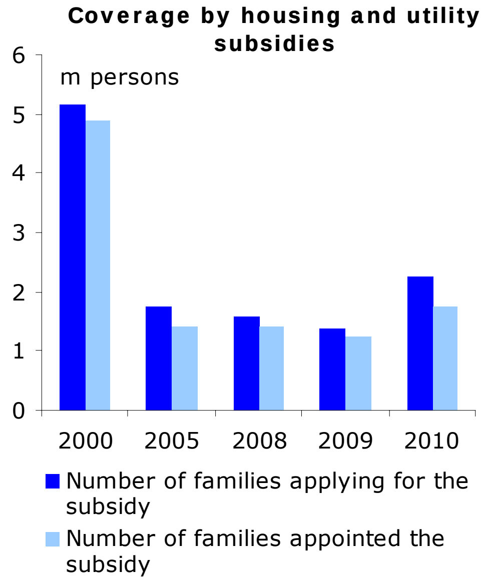
Social standards and minimum wage in 2011. According to the State Budget Law for 2011 general level of subsistence minimum will increase from UAH 894 in January to UAH 953 in December.[xciv] It will grow in line with officially projected inflation at 8.9% yoy in December 2011, thus, remaining close to the levels of 2010 in real terms. Minimum wage will reach UAH 1004 in the end of the year. The first tariff rate in the UTS will be also gradually increased to UAH 654 in December,[xcv] being at 65.1% of minimum wage for entire year. Therefore, it seems that the Government rejected the populistic approach in defining the social standards. At the same time, the Parliament did not increase subsistence minimum likely due to strong coordination with the Cabinet of Ministers.

Pension system: The pension reform remains high in agenda

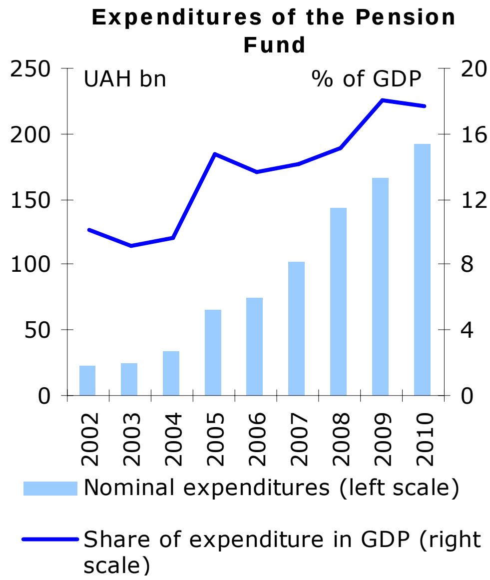
Pension Fund's Budget 2010. The Government approved the budget of the Pension Fund for 2010 only in July envisaging deficit at UAH 28.8 bn.[xcvi] The lion share of the deficit (UAH 26.6 bn) was to be financed at the expense of special central fiscal transfer, while the rest was covered by Fund's account balance available in the beginning of the year. Total revenues were planned at UAH 165.7 bn, including UAH 38.2 bn central fiscal transfer for paying pensions according to special pension programs, retired militaries and judges.



Source: State Budget Laws



Source: Derzhkomstat



Source: Pension Fund, Derzhkomstat

According to the Pension Fund, its own revenues[xcvii] in 2010 were executed at 95.6% of the plan. The under-execution was partly associated with lower than officially expected growth of gross wages and contributions from small entrepreneurs. The central fiscal transfer for financing special pensions was under-executed by 2.0%, while the program envisaging higher pensions to miners was fully financed. The central fiscal transfer for the Fund's deficit financing was executed in full.

Due to lower than planned own revenues, the Pension Fund continued receiving short-term loans from the State Treasury to cover liquidity gaps. The Treasury reports on budget execution lack this information, continuing non-transparent policies in financing pensions. Total deficit of the Pension Fund is estimated at UAH 34.6 bn in 2010.[xcviii]

Pension benefits in 2010. In the State Budget Law for 2010 (see *Fiscal Policy*), the minimum old-age pension was retroactively increased to UAH 695 since January 1, 2010 and UAH 706 since April 1, 2010. As a result, in May and June pensioners received higher pensions as a compensation for lower benefits paid before the approval of the fiscal plan. The minimum pension was then gradually raised to UAH 734 in December. Overall, nominal minimum pension surged by 38.9% yoy on average over 2010. Due to increase in minimum pension average pension reached UAH 1154 as of January 1, 2011,[xcix] being by 11.0% higher than a year before.

Pensions and simplified taxation. In July, the Parliament approved the amendments to the Pension Law,[c] according to which the individuals working under the simplified scheme of taxation were obliged to pay a pension insurance contribution equal to contribution paid from minimum wage at least. Hence, the burden on small entrepreneurs increased, while the Pension Fund received additional revenues.

Pension reform. In December 2010, the Cabinet of Ministers submitted to the Verkhovna Rada a draft law posting changes in the pension legislation. The document envisages an increase in retirement age for women from 55 to 60 years old. The age is to be increased gradually by 0.5-year each year.[ci] The minimum working record and minimum insurance period are also to be increased.

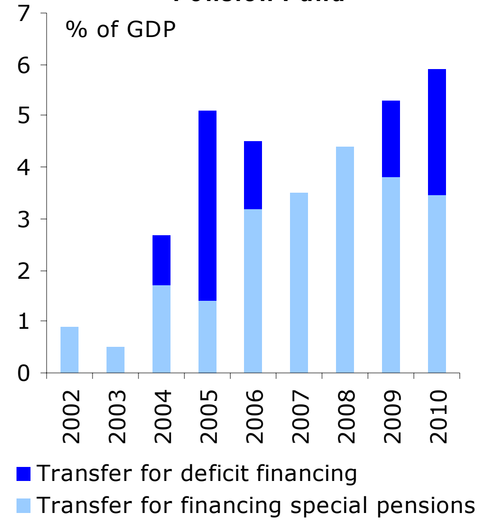
The document also foresees measures limiting the growth in the future Pension Fund's liabilities and central fiscal transfer to the Fund. In particular, it is planned to introduce maximum pension at the level of 12 sizes of subsistence minimum for individuals who lost ability to work. Special pensions for individuals eligible for early retirement will be paid only if these people do not continue work or if they reach statutory retirement age. These norms are likely to be applicable only for new pensioners.

The draft law emphasises the Government plans to introduce the second pillar of the pension system, represented by the Accumulation Pension Fund. It would be implemented only after the Pension Fund's budget is balanced. Taking into account that suggested pension reform is expected to have more medium-term impact, the second pillar is likely not to be an issue for next 2-3 years.

Pension Fund Budget 2011. The deficit of the Pension Fund is expected to reduce to UAH 17.8 bn in 2011 as wage growth will outpace increase in pensions. In particular, minimum pension will not increase in real terms in 2011 contrary to 2010. In nominal terms, minimum pension will be raised by 8.1% yoy on average in 2011 or 9.0% yoy in December. By the end of the year the minimum pension will reach UAH 800.

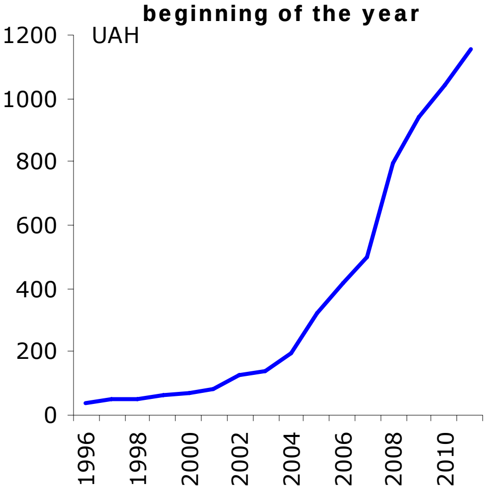
At the same time, total central fiscal transfer to the Pension Fund will remain high at UAH 58.3 bn, accounting for 18.1% of planned central fiscal expenditures. In particular, the part of transfer aimed for financing special pension programs is to be increased by 8.1% to UAH 40.5 bn.

Central fiscal transfer to the Pension Fund



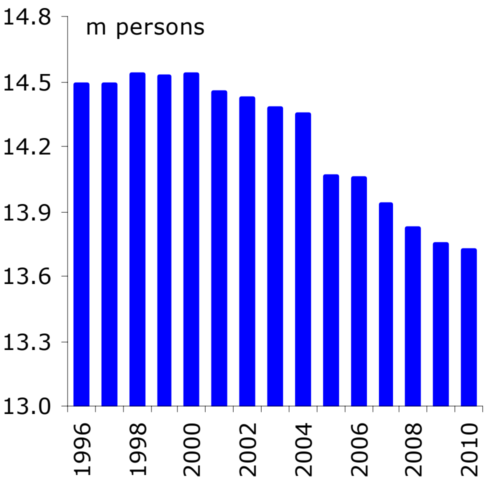
Source: Treasury reports, Derzhkomstat

Average monthly pension, beginning of the year



Source: Derzhkomstat

Number of pensioners



Source: Derzhkomstat

State debt: The Government continued borrowing

In 2010, the limited increase in fiscal revenues and higher government liabilities resulted in further soaring of the state debt. Total – direct plus guaranteed – debt increased by 36% in 2010 to UAH 432 bn (USD 54.3 bn). In relation to GDP it reached 39.5% in the end of 2010 as compared to 12.3% in the end of 2007 and 20.0% in the end of 2008. Even though the debt remained moderate by international standards, the risk of fiscal sustainability intensified.

Domestic borrowings. According to the NBU, the value of domestic state bonds outstanding increased by 91% yoy as of the end of December 2010 to UAH 136 bn. The bonds were issued for financing fiscal expenditures, redeeming previous issues of bonds, reimbursing VAT refunds arrears as well as increasing statutory capital of banks and of the Naftogaz.

Among bonds issued to finance fiscal expenditures and redeem previous issues, 56.7% had a maturity up to one year, 7.6% had a maturity above three years, and other bonds had a maturity from one to three years. Middle-term bonds were mostly issued to finance projects in the framework of preparation for EURO-2012. Reliance on bonds with short-term maturity indicated the government's attempt to shift fiscal gap with hopes for better fiscal situation in near future. However, bonds issued and matured in 2010 were redeemed at the account of new issues. The policy of short-term borrowings is not sustainable unless this debt allows financing reforms ensuring stable increase in fiscal revenues in the future.

During the year, the weighted-average yields declined from over 20% p.a. to as low as 7.9% p.a., signaling about higher government credibility and better economic situation.

In August, the Ministry of Finance issued 5-years VAT bonds, envisaged in the State Budget Law for 2010. These bonds amounted to UAH 16.4 bn were granted to companies with proven VAT refund arrears as of January 1, 2010.[cii] The bonds carry semi-annual 5.5% p.a. coupons. 10% of principal is repaid with each coupon payment. Initially, the VAT bonds had been traded on the secondary market with a 20-percent discount, but it has narrowed later on. Non-resident have been rather active buyers of VAT bonds attracted by high yield and relatively low risk.

The structure of domestic state bonds ownership changed in 2010. The amount of bonds outstanding held by non-residents increased from less than 0.7% to 8.3%. The share of bonds owned by commercial banks increased from 27.1% to 40.2%, signaling about certain crowding-out effect of private borrowings as banks preferred to invest into less risky state bonds rather than into real sector.

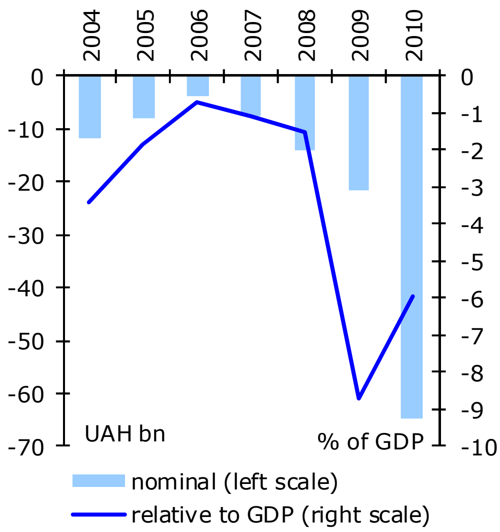
The share of the NBU decreased from 59.7% to 46.5% even though the nominal value of bonds in its portfolio grew by 49.3% yoy in December to UAH 63.3 bn. The strategy and role of the NBU on the domestic state bonds market had changed during the year. In the first quarter, the NBU was active in monetizing state bonds issued in the end of 2009 and in the beginning of 2010 to increase statutory capital of banks and of the Naftogaz. Starting from April, the NBU had declined the nominal value of state bond holdings. Lower level of bonds' monetization is a welcome step on the market.

External borrowings. The large fiscal gap and limited possibilities to accelerate domestic borrowings even further spurred demand for external borrowings, while improved economic outlook and political stabilisation made them possible.

In June, the Government attracted six-month credit at USD 2.0 bn from the Russian VTB to finance fiscal gap until the Government either receives money from the IMF (see *IMF*) or enters international capital markets. This loan was extended in December for another six months despite the fact that Ukraine received the IMF financing.

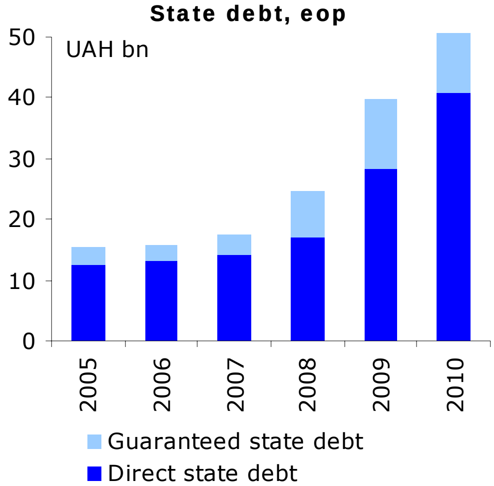
In September, the Ministry of Finance returned to the international capital market for the first time since 2007. It sold 5-year Eurobonds

Consolidated fiscal balance



* without funds for recapitalisation
Source: State Treasury Reports

State debt, eop



Note: not inlcuding loans from State Treasury
Source: State Budget Laws for 2003-2010

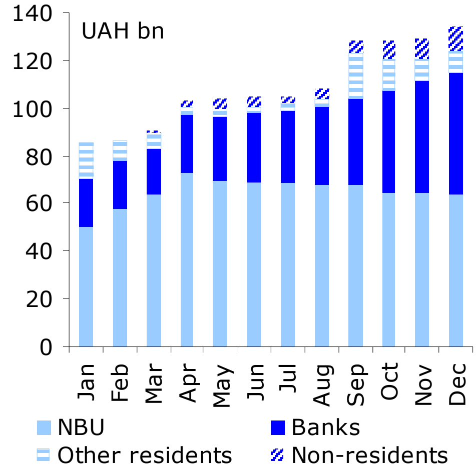
at USD 0.5 bn with yield of 6.875% p.a. and 10-year Eurobonds at USD 1.5 bn with yield of 7.75% p.a. The yields are close to the year 2007 placement yield. The coupon payments on the bonds are due on March 23 and September 23. The yields were lower than for identical Greek bonds indicating relatively strong investors' confidence in Ukraine backed by its higher political stability and better economic situation. Still, the spread with T-bills for 10-year Eurobonds was larger in 2010 than in 2007 reflecting high investors' risk assessment of Ukraine.

In December, the Government rapidly issued 1-year Eurobonds at USD 0.5 bn with yield of 6.7% p.a. without conducting road-show. The urgency might be explained by necessity to redeem Eurobonds issued in Yen in 2006 against the background of later receiving of the second tranche of the IMF loan. This amount allowed the Government to successfully redeem the bonds and pay coupon at total amount of USD 427 bn.

Summing up, the Government continued to quickly aggravate debt. Attracted funds were mostly directed to finance consumption-oriented fiscal expenditures, though some structural reforms were declared to stabilise fiscal situation in the future.

The large share of short-term debt creates risk for fiscal sustainability already in the nearest future. According to the Ministry of Finance, state debt to be redeemed in 2011 amounts to UAH 50.9 bn.[ciii] Besides, debt servicing will reach UAH 21.0 bn or 7.4% of planned central fiscal expenditures.[civ].

Structure of state domestic bonds by holders in 2010*

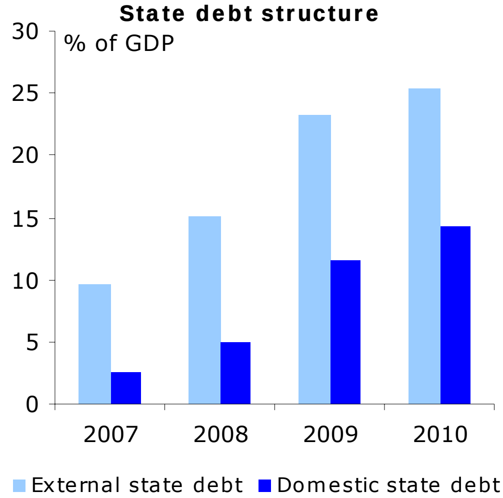


*By principal
Source: NBU

Privatisation: Activation of privatisation

Execution of the Privatisation targets 2010. State Budget[cv] 2010 defined UAH 10 bn as privatisation revenues target. This figure was in line with the assessments of the new the State Property Fund (SPFU) Head Mr. Oleksandr Ryabchenko, appointed in March 2010, and with objects planned for privatisation – energy generating companies and Ukrtelecom. However, slow privatisation processes and shifts in schedule led to summer amendments of the plan, namely its reduction to UAH 6.3 bn.[cvi] From 85 tenders announced in 2010 only 12 resulted in the sale of objects, and 31 from 132 shareholdings offered on the stock exchanges were sold. The most interesting and successful bids were 25.00% of Poltava oblenergo and 25.02% of Prykarpattya oblenergo, which brought UAH 145 m to state coffers. Overall, privatisation plan was executed at 15% of the target in 2010. The sale of Ukrtelecom, expected to secure the execution in the last days of December, did not take place.

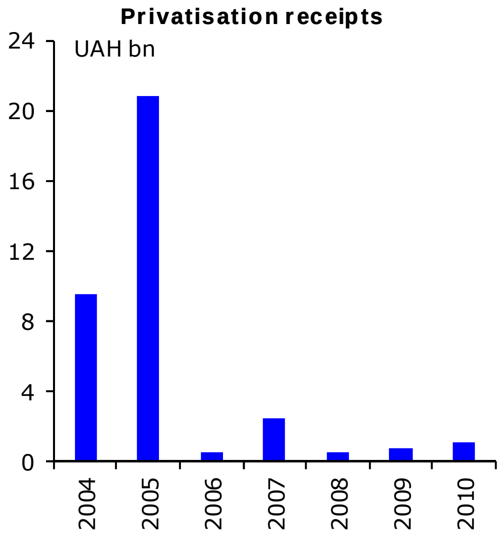
State debt structure



Source: Ministry of Finance reports

Luganskteplovoz reprivatization. The sale of 76.01% stake of JSC "Luganskteplovoz", locomotive producing company, was the first big privatisation auction conducted after the Presidential elections. This case could be used as litmus on transparency of the new privatization policy. In 2009, the 2007 sale of the company to Russian enterprise, Bryansk machine building plant (BMBP), was declared invalid by court, and the enterprise was returned to the state. According to court decision, Ukraine had to return to Brynsk machine building plant USD 58 m, the dollar equivalent of the 2007 sale price. This amount was not transferred to the BMBP by the time of auction. Initially the SPFU had registered five bidders but three of them were disqualified few days before the auction. Among the participants there was the previous owner, who offered UAH 10 m premium to the starting price of UAH 400 m and was declared the new winner. After auction, Ukraine remained owing UAH 48 m to the BMBP. However, the BMBP did not meet the deadline for money transfer and the SPFU claimed in court to cancel the deal. After series of cross claims, sides signed amicable agreement of offsetting debts. The reprivatisation of the plant did not turn to be more profitable and indicated that basically privatization policy in Ukraine has not changed with the new Government and still is not strategically targeted and streamlined.

Privatisation of the Ukrtelecom. Another example of still non-transparent privatisation in Ukraine was the auction for the sale of the largest fixed line telecommunication operator – Ukrtelecom. The State Property Fund of Ukraine estimated the start price for the shareholding of 92.8% on the level of UAH 10 bn and planned the auction for December 28.[cvii] According to market, Mobile Telesystems (Russia) and System Capital Management (Ukraine) could compete for the enterprise. Investment conditions entitled the new owner to cover debt of the Ukrtelecom, to establish of the special state communication system and to invest around UAH 450 m into the enterprise. Although during the preparation for the tender the SPFU declared six interested companies, in reality only one paid participation guarantee and, thus, applied – a daughter company of Austrian concern Eris - ESU with a bid, only by UAH 10 exceeding the start price of the SPFU. According to the Ukrainian legislation, SPFU selected independent assessment company to set the price of the object until February 2011. After the estimation, the ESU paid UAH 10.5 bn for the company in several tranches in the spring of 2011.



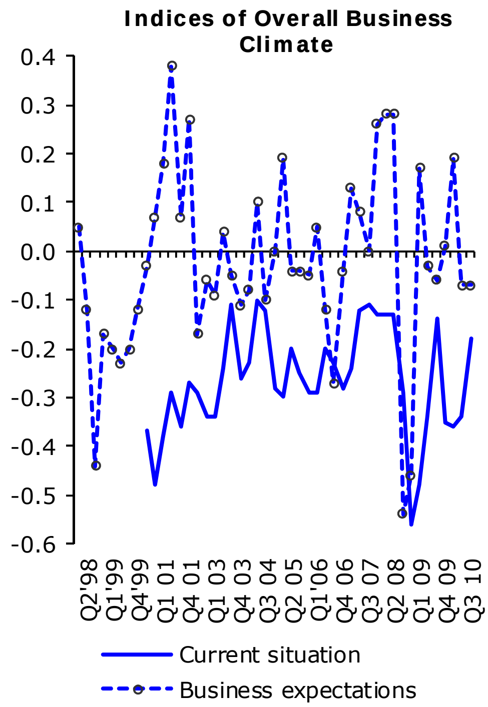
Source: State Treasury of Ukraine

Surpisingly, no disputes concerning transparency and efficiency of the sale followed. Thus, the blue chip, which has been the lot for a couple of years was practically sold without competition, proving the traditional Ukrainian privatisation style.

Privatization plans 2011. According to the State Budget Law for 2011,[cviii] privatisation receipts are set at UAH 10 bn. This amount was received in 2011 due to successful privatisation deal for Ukrtelecom. December annulment of President's Order envisaging ban on the sale of strategic enterprises before adaptation of Privatization Program[cix] opens the way for other large privatisation deals. Thus, such blue chips as Turboatom, Odessa by-port plant and several energy distribution companies might find their private owners already in 2011. The conclusion of the purchase-sale agreement for the Ukrtelecom immediately result in complete execution of the privatisaion receipts plan.

Business climate: Dynamics of estimations and expectations of business leaders in 2010

In Ukraine, several research organizations conduct surveys of entrepreneurs to construct a business confidence index. Quarterly business tendency survey, conducted by the IER, is the oldest. The analysis presented below is based on the results of this survey.



Source: IER Surveys

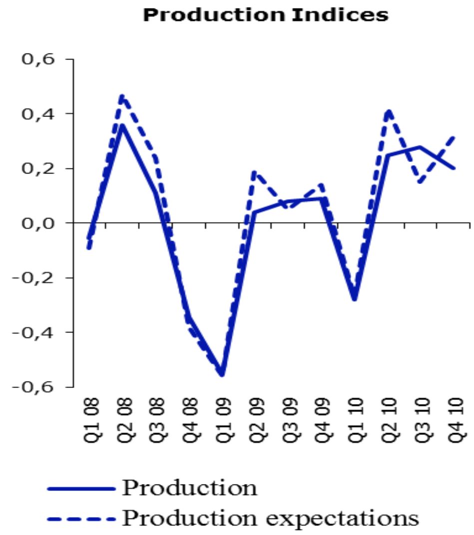
Business expectations. In the beginning of 2010, business expectations for next six months improved. The index of expected business climate, which reflects the respondents' assessment of the future business climate, has increased from 0.06 in October 2009 to 0.01 in February 2010. In April, the trend on expectations improvement continued. Index of expected changes in business environment has increased by 18 points (from 0.01 in February to 0.19 in April). However, after six months of improved expectations the evaluation of the business climate has not improved. It remained from the beginning of the year without significant changes: the value of the index was -0.35 in February, -0.36 in April, and -0.34 in July.

Already in July, managers' expectations about changes in business environment in the next six months deteriorated. The index of business expectations reduced by 26 points (from 0.19 to -0.07 in July). Simultaneously the share of "optimists" also declined (from 32.2% to 17.1%), while share of "pessimists" increased (from 16.7% to 31.8%).

In October, the quality assessment of current business climate significantly improved as compared to July: the value of the index has increased by 16 points (from -0.34 to -0.18). However, one should note that the share of those, who reported that the business environment is unfavourable, was 31.2% and prevailed over proportion of those who considered it favourable by almost 25%. Expectations of business for the improvement of the overall economic situation in next six months remained without significant changes in 2010 (-0.07 to -0.07 in October and July).

Production figures. In the first quarter of 2010, as it was previously expected by managers, there was a significant slowdown of industrial production growth as compared to the IV quarter of 2009. The value of the production index decreased significantly from 0.09 in the IV quarter to -0.28 in the first quarter. At the same time, the growth of business optimism in April significantly affected the production plans of enterprises: the index of expected production increased from -0.27 in the first quarter to 0.42 in the second quarter. Every second respondent (51.4%) planned to increase output in the second quarter compared to I

Optimistic production plans of the beginning of the year have already come true in the second quarter. Then, as expected by the managers, there was a significant improvement of main indicators of enterprises (production, sales, employment, etc.). In particular, there was an increased growth rate of industrial production, which was reflected in increasing of the production index from -0.28 in the first quarter to 0.25 in the second. At the same time production expectations - particularly in the third quarter managers of enterprises expected decline in production activity as compared to the second quarter. The index of expected production decreased from 0.42 in the second quarter to 0.15 in the third.

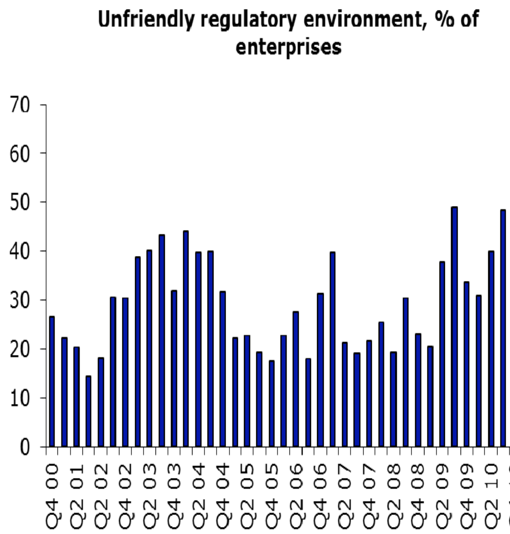


Source: IER Survey

According to managers' estimations, in the third quarter production volumes have not changed significantly compared to the second, and in the fourth quarter, managers expected slight increase in manufacturing activity. The index of production expectations increased from 0.15 in the third quarter to 0.32 in the fourth quarter.

Regulatory climate. Assessment of regulatory climate by managers of industrial companies has significantly deteriorated during 2010. If in February 2010, 31.1% of managers believed that the regulatory climate is a significant barrier for activity, only 39.9% thought so in April. This share increased further to 48.5% in July. The survey in October showed stabilization of this indicator at 48.3%.

The frequency of negative evaluations of the regulatory climate increased among managers of enterprises of all sizes. In groups of medium and large enterprises the number of managers, according to whom the regulatory climate is a major obstacle activity, has been increasing every quarter and reached a peak in October, when 45.7% of managers of medium-sized enterprises and 52.2% of managers of large enterprises reported this problem. The indicator value for small firms has been increasing during first three consecutive quarters (29.3%, 47.4% and 53.8%). However, in October there was a decline in the number of managers who claimed the regulatory climate as one of major impediments to business development (to 48.1%). This happened due to a significant reduction in values of two out of three components of the combined index of "unfavourable regulatory climate", namely: frequent changes in economic legislation (from 18.8% to 8.6%) and corruption (from 17.9% to 8, 6%).



Source: IER Survey

Loans market. The climate in the banking loans market in 2010 was characterized by increase in formal credit supply, on the one hand, and decline in their real availability, on the other. The share of managers who believed that banks were willing to provide short-term loans to enterprises such as their, has been growing on a quarterly basis and in October reached of 57.2%. The value of respective indicator for long-term credits increased from 40.3% in April to 44.2% in July and to 53.6% in October.

In February 2010, the availability of loans for businesses, according to managers, increased as compared to October 2009, albeit in April it decreased from 34.2% to 26.5% for short-term loans, and from 26.6% to 21.2% for the long-term. In July, the availability of loans to enterprises increased somewhat. However, in October it declined again: from 27.7% to 23.4% for the short-term loans, and from 24.4% to 21.8% for the long-term loans.

Investment activities. The results of the survey on the investment activities of enterprises, which was conducted in January and

February of each year, showed that among all the surveyed managers more than half (54.3%) did not plan to invest in 2010. Only 45.7% of managers planned to invest during 2010, what was not much different from 2009, when the share of firms that made investments accounted for 44.7% of respondents.

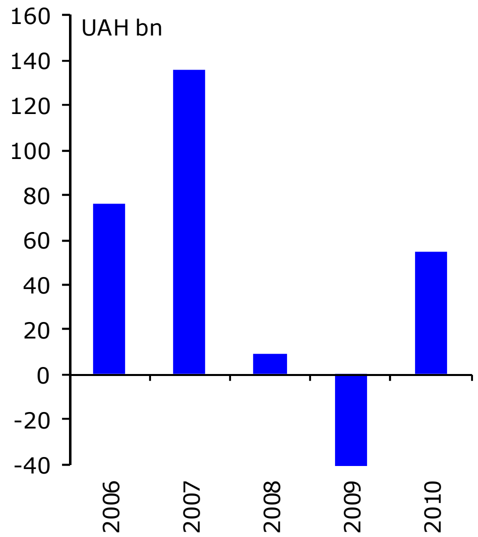
Among managers of enterprises who planned investments for 2010, most respondents (59.7%) noted that the number of investment would not change as compared to 2009, 22.0% believed that they would be lower than last year. Only 18.2% of managers planned to spur investment. Increased investment planned only managers of small businesses, while managers of medium and large enterprises did not intend to increase the volume of investments as compared to 2009.

These results correspond well with official statistics (see *Investments*). During the first nine months of the year real investment in fixed assets declined by 2.9% yoy as compared to the previous year.

The vast majority of managers assessed the purchase of equipment in 2010 as unfavourable (73.3%). Although this share declined as compared to 2009, which was considered as unfavourable period by 88.6% of managers, it remained higher than in early 2008 (66.3%). At the same time, in 2010 the share of managers, who assessed the current period as a more or less favourable for the purchase of equipment, more than doubled (from 10.9% in 2009 to 24.5% in 2010).

According to the survey, three major impediments for investment planning were reported insufficient income (47.7%), unstable political situation (35.0%) and difficulties in obtaining loans (27.2%).

Financial result of enterprises' general activity



Source: Derzhkomstat

Financial state of enterprises: Renewal of positive economic performance

After the losses, experienced by majority of the Ukrainian enterprises in 2009, the year 2010 was marked by the revival of economic activity and positive financial results in almost all sectors of the economy. Over the ten month of 2010, the financial results of domestic enterprises reached UAH 49.7 bn growing by UAH 65.3 bn compared to the same period in 2009. The ratio of profitable and loss making enterprises did not change as of 2009, what indicates, that large profit making industrial enterprises resumed their activity, whereby small businesses might not overcome the crisis.

Thanks to renewed export growth following the improvement of economic conditions in the world, industrial sector registered large increase in profits. Pretax profit of industrial firms reached UAH 26 bn between January and November 2010 compared to UAH 0.3 bn losses a year before. Performance of financial sector that reported the largest losses in 2009 (UAH 27.3 bn) also improved significantly mainly thanks to operations of insurance and investment companies and the sector's pretax profit reached UAH 9.1 bn in 2010. The only loss-making sector that did not recover in 2010 were construction industry and provision of communal and individual services. Low real demand on the housing market accompanied by weak bank loans as well existence of the large amount of available newly constructed unsold housing doesn't allow construction companies to resume their activity.

Companies in industrial Dnipropetrovsk, Donetsk and Zaporizhzhya regions and economically diversified Kyiv city led the economic recovery in 2010 bouncing back after being hit the most by the world economic crisis. The highest cumulative losses are reported by firms in Kharkiv and Lugansk regions, although their economic performance slightly improved in comparison with the previous year (UAH 1.8 bn and UAH 2.8 bn respectively). Aggregated financial results of enterprises in Ivano-Franskivsk region even worsened compared to 2009 by UAH 0.6 bn. Profitability of Ivano-Frankisvk's enterprises dropped by 2.4% and is among the lowest in Ukraine (0.4%).

Inflation: Consumer inflation returned to single digits in 2010

In 2010, consumer inflation returned to single digits reaching 9.1% yoy in December as compared to 12.3% yoy in December 2009. Deceleration was broad-based as price increases in main components of CPI were smaller than in previous year. The only exception was category 'housing, utilities and other fuels', flagging high growth caused by one-off 50% increase in natural gas tariffs paid by households.

Food, alcohol and tobacco, and utility price increases were key contributors to CPI growth. Alcohol and tobacco price grew by 22.1% driven by several hikes in excise rates on these products. Food prices grew at 10.7% yoy, which is slightly faster than the CPI, making the largest contribution to CPI growth due to 50% share in CPI basket. In 2010, food prices were more volatile than before demonstrating swift increases in spring and autmn and slowdown in summer.

On the demand side, income growth created some inflation pressure. Nominal disposable income of households grew by 28.1% in 2010 as compared to 4.2% growth in 2009. However, this pressure was moderated by high savings rate. Households continued to repay loans in foreign currency, as well as increased bank deposits and foreign cash holdings. Overall households saved UAH 161 bn in 2010 which is twice the 2009 amount.

On the supply side, the most of changes pushed inflation up, but more slowly than could be expected. Energy costs and prices for imported commodities grew at limited pace having contained impact on prices. Growth in social standards did not result in proportional increase in labour costs. Among the most prominent impacts, lower harvest in 2010 contributed to higher prices on agricultural products.

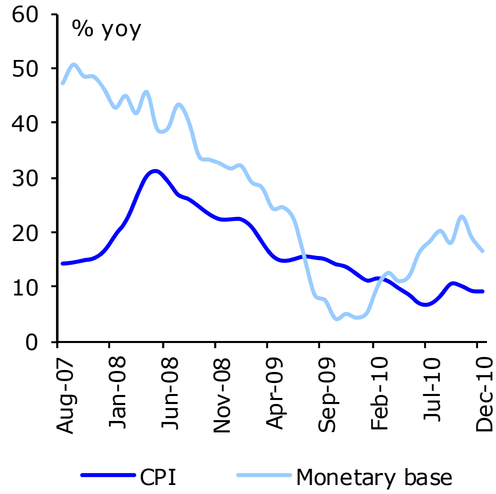
Government tried to limit price growth keeping electricity prices for population fixed and restricting increases in other utility tariffs. It also continued to apply formal price controls, as well as increased scrutiny of competition authority and informal pressure to limit prices increases. Government intervention led to lower CPI growth in 2010 but aggravated inflation pressure for future years.

Monetary policy: Money supply returned to growth

Money supply returned to growth in 2010. In 2010, money supply (M3) increased by 22.8%, while monetary base by 15.8% yoy. The growth was mostly fuelled by NBU interventions on foreign exchange market and conversion of external government borrowing into national currency. In total, the NBU bought over USD 6 bn from the government and banks in 2010. However, the purchases were unevenly spread over the year as the NBU made net purchases of foreign currency from March to August while selling foreign currency in other months. As a result, bank liquidity varied from UAH 15-20 bn in January and December to maximum of UAH 34 bn observed in July. In addition, the NBU purchased over UAH 22 bn of government bonds and transferred UAH 12 bn of seigniorage profits to the government. Thus, the NBU monetary policy was in great part subordinated to exchange rate and public debt policies.

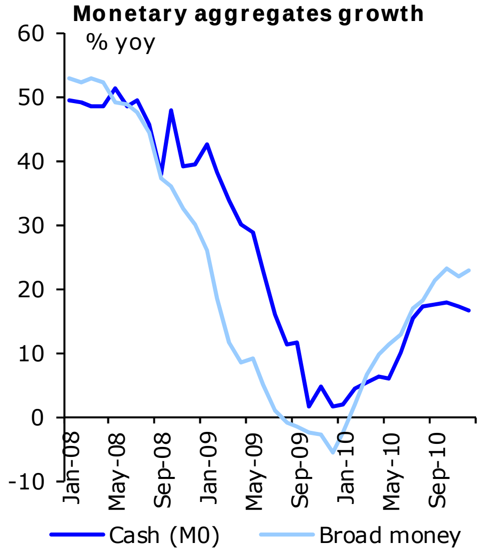
However, the NBU actively used other monetary instruments to offset the infusion of liquidity and limit volatility. In particular, the NBU sold certificates of deposit (CDs) to banks, decreased refinancing loans outstanding, and sold part of government bonds in its portfolio. Among those, the CD issuance was the main instrument used to regulate bank liquidity. In 2010, bank liquidity improved as deposits returned to banks and repayments on loans increased. Consequently, refinancing offered by the NBU became unattractive to banks as rates were much higher than those offered at inter-bank market. The NBU issued UAH 243 bn of CDs in 2010, including UAH 38 bn of CDs with maturity over 30 days and UAH 82 bn of CDs with maturity between 8 and 29 days. In response to changes in bank liquidity, the NBU varied interest rates and maturities of CDs offered. As a result, amounts of CDs outstanding fluctuated from record

CPI and monetary base development



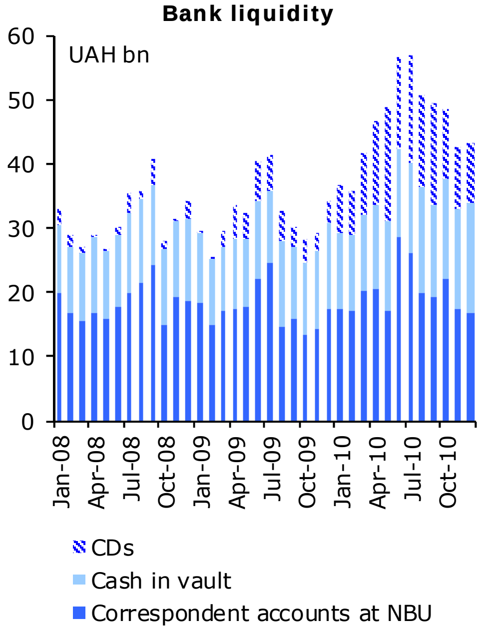
Source: Derzhkomstat, NBU

Monetary aggregates growth



Source: NBU

Bank liquidity



Source: NBU

levels over UAH 20 bn on some days in June and July to below UAH 10 bn in the beginning and in the end of the year.

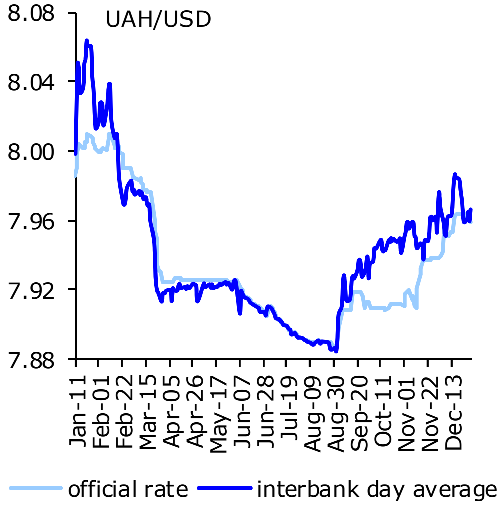
The NBU also tried to increase role of government bonds in monetary policy. It is only natural as nominal value of domestic government bonds (OVDP) outstanding was UAH 136 bn including 64.2 bn of government bonds owned by the NBU by the end of the year. The NBU holdings originate mostly from quasi-fiscal activities by the government in 2009 but it continued to buy OVDP in 2010. The role of the NBU gradually decreased as share of the NBU holdings decreased from over 70% in January and February to less than 50% in November and December. Usefulness of the NBU portfolio in monetary policy is somewhat limited as it is composed in large part from bonds with maturity over 5 years that are currently illiquid. As a result, outright sales of government bonds were limited to UAH 7.4 bn including UAH 3.3 bn in September. However, the liquidity of the bond is less relevant in repo transactions and the NBU used government bonds in direct and reverse repo transactions and sales with indefinite commitment to repurchase. The role of government bonds in monetary policy is likely to grow in next years.

There were only few instances when the NBU financed banks through regular channels in 2010. Therefore, three changes of discount rate in summer were mostly symbolic. Cumulatively discount rate decreased from 10.25% p.a. to 7.75% p.a. In 2010, the NBU provided over UAH 3 bn in stabilization loans to problem banks, and UAH 1 bn to support EURO-2012 football championship projects. It also extended repayment for some refinancing loans issued in 2008 and 2009. As a result, refinancing loans outstanding decreased only by UAH 12 bn by November 2010, despite the fact that the NBU expected to receive UAH 25 bn in repayments and UAH 41 bn of refinancing loans were due in 2010. The NBU kept emergency liquidity supplied in the height of the crisis in the banking system.

The NBU did not change reserve requirements in 2010 formally. Nevertheless, in May the NBU demanded that banks keep entire rather than half of required reserves at special account. Thus, all required reserves were frozen to limit bank liquidity. However, this measure did not have the desired effect as banks were allowed to include government bonds issued to finance EURO-2012 in reserves. As a result, out of UAH 12.2 bn reserves required by the end of the year only UAH 7.7 bn were frozen.

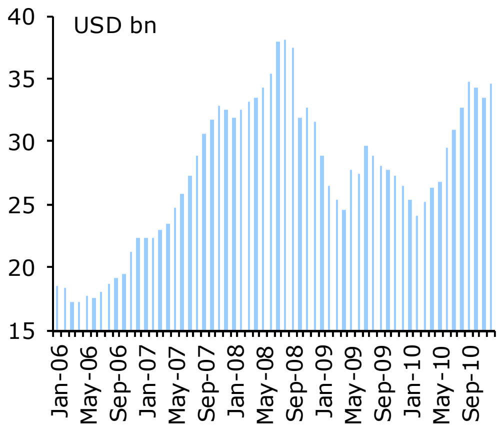
In sum, the NBU monetary policy was moderately expansive in 2010.

Exchange rate in 2010



Source: NBU

International reserves



Source: NBU

Exchange rate policy: Exchange rate was stable in 2010

UAH/USD interbank exchange rate remained generally stable in 2010. It appreciated a little from UAH/USD 7.99 at the end of 2009 to UAH/USD 7.97 at the end of 2010 with average rate of UAH/USD 7.94. Average daily exchange rate remained in tight range of UAH/USD 7.88-8.06 throughout the year with little day-to-day changes. The NBU intervened on the market to preserve exchange rate stability. However, direction of interventions varied as balance of supply and demand changed throughout the year. The year could be tentatively divided into three distinct periods.

In January and February 2010, foreign currency supply was lower than demand mostly due to elevated demand for foreign cash against the background of presidential elections. Increased hryvnia liquidity created additional pressure. Slight excess of supply over demand in cashless segment of the market was not sufficient to cover demand for foreign cash. As a result, the NBU sold USD 1.6 bn to support exchange rate while hryvnia weakened slightly reaching UAH/USD 8.06 in late January. However, national currency returned below UAH 8 per USD by the end of February.

Between March and August, inward capital flows increased as political stability returned and economic prospects improved. Export revenues also grew significantly. Moreover, cash foreign currency became less popular as savings vehicle. As a result supply of foreign currency was significantly larger than demand. In response the NBU allowed hryvnia to appreciate slightly from UAH/USD 7.98 in the beginning of March to UAH/USD 7.88 by the end of August. In addition, the NBU bought USD 5.1 bn in interventions to prevent hryvnia from appreciating further.

Between September and December demand for cash foreign currency increased significantly again. Gross purchases of cash foreign currency were USD 12.9 bn over this period as compared to USD 13.4 bn over the rest of the year. Spike in demand was probable partly caused by the increased demand from shadow economy fuelled by concerns over tax reform. Demand for foreign currency to finance imports and repay external debts also increased. As a result hryvnya weakened slightly. Although the NBU sold and purchased foreign currency during the period it again became the net seller of the foreign currency. Overall net interventions during the period were USD 2.2 bn.

Financial markets: Banking system had mixed performance in 2010

Banking. Banking system finished the year of 2010 with both good and bad results. On the bright side, central bank took steps to reduce number of problem banks leaving only four banks under temporary administration as compared to 12 in the beginning of the year. Seven small banks and Ukrprombank were liquidated in 2010 while several others resumed normal operations. More banks were incorporated as public joint stock companies increasing transparency of their operations.

Financial state of banks improved as banks were able to decrease loan losses and contain interest costs. According to financial results of banking sector 133 out of 175 Ukrainian banks reported pre-tax profits including 12 out of 17 largest banks. For comparison only five of the largest banks were profitable in 2009.

Most banks successfully increased deposits from households and legal entities in 2010 including 15 out of 17 largest banks. Overall bank deposits grew by 26.4% in 2010. Bank deposits increased their role in bank liabilities as bank liabilities grew only by 5.1% yoy Moreover banks were able to contain interest costs. Despite growing deposit base banks actually spent less on interest thanks to falling interest rates. In 2010 interest expenditures decreased by 6.0%.

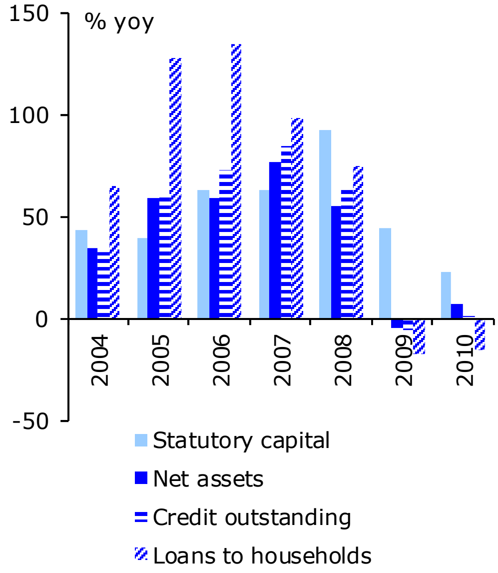
As a result most banks retained high liquidity with 14.0% of total bank net assets as of January 1, 2011 reported as money and money equivalents. Although good liquidity was not uniform throughout the banking sector 116 banks had over 10% of assets invested in money and money equivalents including 29 of 39 largest banks. Banks also used increased funds to repay external debt and increase lending to companies in national currency. Loans to legal entities in national currency grew by 13.5% yoy in 2010. However loan growth in individual banks varied widely and only five banks were responsible for most of the increase in corporate lending.

Banks continued to lend mostly to companies working in trade and manufacturing but loans to extractive industry and transport increased their share in the total. Also banks increased maturity of the loans provided as corporate loans in national currency with maturity over five years grew by 48% in 2010.

On the negative side, NBU so far failed to resolve Nadra and Rodovid banks that despite large write-offs and halt in lending were still 11th and 20th largest banks in Ukraine by assets as of January 1, 2011. Although government recapitalized Rodovid bank by UAH 7.8 bn in 2009 this bank continued to make losses in 2010. As it had very few interest bearing assets and high loan losses it lost almost all of the new capital by the end of 2010. Nadra bank had better core business with net interest income of UAH 1.4 bn but loan loss provisions also ate most of its capital.

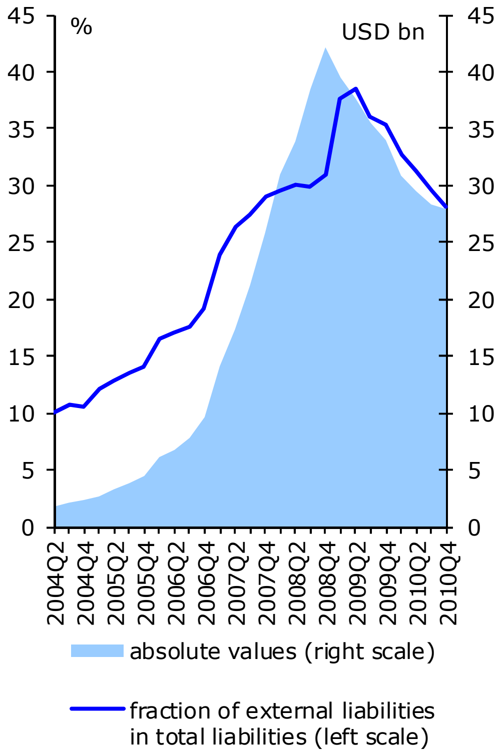
Overall, banking sector lost UAH 12.1 bn between in 2010 due to limited interest income and high loan loss provisions. Interest income declined by 4.6% yoy due to lower interest rates and lacklustre

Growth rates of selected indicators of bank's activity



*banks finished 2009 with UAH 28 bn of loss
Source: NBU

Foreign liabilities of banking sector



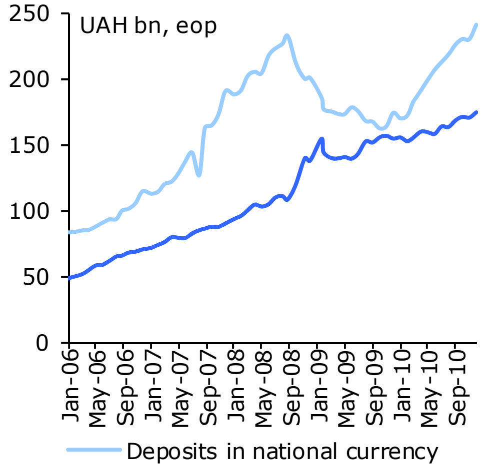
Source: NBU

lending activity. Although most banks reported profits a number of banks formed large loan loss provisions leading to aggregate losses in the banking sector. Also several banks that have low ratio of capital to assets reported some of the lowest loan loss provisions in the banking sector. It means that they may have understated loan losses to comply with capital adequacy requirements. Overall loan loss provisions reached 18.6% of total loans by the end of December but different banks reported different ratios. Out of 39 largest banks ten banks reported provisions of less than 10% of loans and twelve had provisions of over 25% of loans. High loan loss provision may be explained by rigid policy that prevented write-offs of hopeless loans and growing stockpile of problem loans. New rules may simplify write-offs in 2011.

According to the NBU share of overdue loans in loans outstanding increased to 11.2% in December 2010 as compared to 9.4% in December 2009. Share of overdue loans was even higher for loans to nonfinancial corporations where it grew from 11.3% in December 2009 to 13.1% in December 2010. In Companies in most economic sectors had significant trouble paying back loans but magnitude of the problem varied. Share of overdue loans ranged from 4-6% in professional services and extractive industry to 10-14% in transport, manufacturing and trade to 18% in construction and real estate operations. Large share of overdue loans to nonfinancial corporations may be attributed to limited economic growth, large scheduled payments(due to deficient restructuring in previous year) and imperfect legislation that allows some debtors to avoid payment.

Overall banking sector stabilised and showed signs of recovery in 2010. However lending remained subdued, a number of banks remained in difficult financial state and problem of bad debt in bank books became more severe.

Bank deposits



Source: NBU

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i Cabinet of Ministers Decree No.938 from October 4, 2010

ii Getreideexportquoten: Zum Umgang mit Chancen und Verantwortung. Ausgabe 28, Dezember 2010. Newsletter, Deutsche Beratergruppe

iii Cabinet of Ministers Decree #1182 from December 6, 2010 that envisaged the extension of the quotas till March 2011 (with addition 500 thds tons for wheat and 1 mln tons for corn allowed for export)

iv Cabinet of Ministers Decree No. 368 from May 12, 2010 and No. 346 from May 19, 2010

v The Law of Ukraine "On the Tax Code" No 2755-VI as of December 2, 2010. Point 15 of the Section 2 of Transition Provisions.

vi For households that consumed no more than 2.5 tcm of gas monthly and have a gas meter

vii Comprised according to the national accounting standards.

viii This amount is a composition of 11 bn cm of gas main volume transferred to Naftogaz and 1.1 bn cm as penalties.

ix The Cabinet of Ministers Order No 775 as of June 10, 2009 (cancelled by the Cabinet of Ministers Order No 547 as of July 05, 2010)

x The Law of Ukraine No. 2467 "On principles of operations on the natural gas market" from July 8, 2010

xi Directive 2003/55/EC and EU Regulation 1775/2005

xii The Law of Ukraine No. 0198 "On ratification of Protocol on Ukraine's accession to the Treaty establishing the Energy Community" from November 11, 2010

xiii Set up by the Law of Ukraine #1164 as of March 19, 2009

xiv Resolution of the MTCU, No. 19, January 21, 2010.

xv Resolution of the MTCU, No. 128, March 10, 2010.

xvi Resolution of the MTCU, No. 521, July 23, 2010.

xvii Resolution of the MTCU, No. 851, November 25, 2010.

xviii Changes and amendments to the Tariff policy for 2009// http://uz.gov.ua/index.php?m=info.normdocs.tarpolmain.tarpolUZ2007.izmUZ2007&f=Doc.View&p=tpuzzminy.0&lng=uk; Changes and amendments to the Tariff policy for 2010//

http://uz.gov.ua/index.php?m=info.normdocs.tarpolmain.tarif_uz_2010.zminy_dop_2010&f=Doc.View&p=zminy_dop_2010_.0&lng=uk

xix Resolution of the MTCU, No.881, December 7, 2010

xx Decree of the CMU, No. 397, June 2, 2010.

xxi Decree of the CMU, No. 925, October 14, 2008.

xxii Decree of the CMU, No. 226, February 25, 2009 has been voided.

xxiii Resolution of the MTCU, No. 669, September 15, 2010

xxiv https://tender.me.gov.ua/

xxv Materials of the information agency Cbonds// http://www.cbonds.info

xxvi Press-service of UZ// http://www.uz.gov.ua/?lng=uk

xxvii In 2010, new terminal F was opened in Boryspil, and great progress in runways renovation was achieved in Donetsk, Lviv and Kyiv.

xxviii The Law, No. 2404-VI, July 1, 2010 became effective on October 31, 2010.

xxix Boryspil International Airport and refuelling companies were fined by the AMC for monopolistic abuse, which resulted in high fuel prices in Ukrainian airport comparing to others.

xxx In April, the AMC stopped different pricing in the port Yuzhnyy. Also, in summer the AMC obliged different regional railway companies to reduce overstating fees for tickets work.

xxxi In autumn 2010, the AMC protected fair competition between private and public operators when allowed private agrarian company Nibulon to develop its trans-shipment complex in Mykolaiv sea port. In airports sector, list of services provided by natural monopolies was specified by the Decree of the CMU, No. 590, July 14, 2010. So, now the CMU can easier regulate them and stimulate competition in any other airport segment.

xxxii The share of three companies on the market was 48.5% in 2009.

xxxiii The Order of the CMU, No. 2174-p, October 20, 2010

xxxiv The Order of the CMU, No. 2264-p, December 15, 2010.

xxxv Press-service of the MTCU// http://www.mtu.gov.ua/uk/news/2010-06-15/17924.html

xxxvi Resolution of the MTCU, No.427, from July 2, 2010.

xxxvii The Order of the President, No. 1085/2010, December 9, 2010.

xxxviii Resolution of the NCCR, No.52, February 4, 2010.

xxxix Order of the AMC, No. 305-p, June 24, 2010.

xl The fees constituted 0.18-0.25 UAH/min for access to fixed-line networks, and 0.35-0.40 UAH/min for access to mobile networks// Resolution of the NCCR, No.299, July 1, 2010.

xli Resolution of the NCCR, No.497, November 4, 2010

xlii The NCCR now can determine (without the AMC) operators with SMP, i.e. operators whose share in total revenues from traffic transmission services on this market is more than 25%.

xliii Law of Ukraine, No. 2751-VI, December 2, 2010.

xliv Law of Ukraine, No. 2752-VI, December 2, 2010.

xlv Resolution of the NCCR, No.1607, July 23, 2009.

xlvi Press service of the NCCR// http://www.nkrz.gov.ua/uk/activities/news/1280230559/

xlvii Report of the NCCR// http://www.nkrz.gov.ua/uk/activities/1238055440/

xlviii Resolution of the NCCR, No.1789, December 10, 2009.

xlix Resolution of the NCCR, No.348, July 29, 2010.

l Decree of the CMU, No. 890, September 29, 2010.

li This principle means that different technologies offering similar services should be regulated in similar manner. Such regulation balances costs and benefits of both providers and consumers as companies in equal market conditions compete and customers can benefit from wider choice and lower prices// ICT Regulation Toolkit// http://www.ictregulationtoolkit.org/en/Section.1833.html.

lii Earlier they paid only 6% of license fee for telephony.

liii Law of Ukraine, No. 2608-VI, October 19, 2010.

liv Resolution of the NCCR, No.174, April 15, 2010.

lv Resolution of the NCCR, No.363, August 5, 2010.

lvi Law of Ukraine, No. 2392-VI, July 1, 2010.

lvii Resolution of the NCCR, No.590, December 23, 2010.

lviii Resolution of the NCCR, No.483, October 28, 2010.

lix The Decree of the CMU, No. 321, April 23, 2010.

lx Law of Ukraine, No. 2755-VI, December 2, 2010.

lxi Press service of the AMC.

lxii Press service of the AMC

lxiii http://www.mintrans.gov.ua/uk/news/17163.html

lxiv Two tranches were made in February and in May 2010

lxv In October, it raised UAH 152.6 m with a 17% coupon rate through public offering of bonds and in December - UAH 200 m in credit.

lxvi http://www.ukrtelecom.ua/about/finance/financial_reports

lxvii Decision of the AMC, March 9, 2010.

lxviii It accounts for 45.3% of Ukrainian mobile market by number of subscribers (as of December 2010).

lxix Decision of the AMC, April 22, 2010.

lxx Decision of the AMC, October 19, 2010

lxxi District heating, water supply and wastewater treatment services

lxxii Law of Ukraine On National Regulatory Commission for utilities market of Ukraine, No 2479-IV, 09.07.2010

lxxiii There are more than 500 district heating companies and more than a thousand water companies in Ukraine the tariffs for services of which are going to be set by the commission. To do that one needs significant human as well as financial resources. Neither of that is foreseen. For the reference, the UK's water regulator performs tariff regulation for about 30 companies with 200 people of staff and app GPB 18 m a year budget.

lxxiv Another reason for sharp increase in growth of real disposable income is likely attributed to the methodological changes applied by the Derzhkomstat.

lxxv In 2009 average wage declined by 9.2% in real terms.

lxxvi The unemployment rate defined according to the ILO methodology declined from 9.8% of working able individuals in the first quarter of 2010 to 8.2% in the third quarter.

lxxvii In December 2008 the Parliament introduced variety of measures related to labour market, which complicated registration of people as unemployed and envisaged harder rules concerning job seeking, participation in public works, retraining, etc. The list of reasons for deprivation of the status of unemployed was enlarged. Some impediments for the registering as unemployed were introduced for rural population (see *Supplement to the MEMU, No.5-2009*).

lxxviii According to the Law on Remuneration of Labour (No. 108/95 from March 24, 1995) companies of all ownership type should pay wages according to the tariff scale. The tariff scale is defined by enterprises in the form of set of coefficients. The wages to employees with different qualification are defined as coefficients multiplied by the base (first) tariff rate. The higher coefficient corresponds to higher qualification.

lxxix Minimum wage accounted for 35.1% of nominal average wage in December, 2010.

lxxx The planned deficit does not include funds for banks recapitalisation.

lxxxi The Law Of Ukraine *On the State Budget for 2010*, No.2154-VI, from April 27, 2010

lxxxii Law of Ukraine, No. 2275-VI, from May 20, 2010

lxxxiii The Law of Ukraine, No. 2461-VI, from July 8, 2010

lxxxiv At the same time, there were cases when business has announced about abuse of power by tax authorities, which rejected accepting tax declaration.

lxxxv Annual plan of revenues from sale of military surplus were at UAH 4.1 bn.

lxxxvi No. 2456-VI from July 8, 2010. The first Budget Code was approved in 2001.

lxxxvii Protected spending items include wage and pension payments, social assistance, etc. These are primarily recurrent fiscal expenditures.

lxxxviii Law of Ukraine, No. 2856-VI, from December 23, 2010

lxxxix Law of Ukraine, No. 2856-VI, from December 23, 2010

xc See Supplement to the MEMU No.12 (122), December 2010.

xci The Law of Ukraine "On the Amendments to the State Budget Law for 2009", No.1715-IV, from November 6, 2009

xcii The Resolution of the Cabinet of Ministers, No. 337, from May 12, 2010; Resolution of the Cabinet of Ministers, No. 1056, from November 17, 2010

xciii The Law of Ukraine On Unified Social Contribution, No. 2464, from July 8, 2010

xciv The Law of Ukraine On the State Budget for 2011, No. 2857-VI, from December 23, 2010

xcv The Resolution of the Cabinet of Ministers, No.1212, from December 29, 2010

xcvi Resolution of the Cabinet of Ministers, No.626, from July 21, 2010

xcvii The major source of own Fund's revenues are pension contributions paid by employers and employees.

xcviii The estimates are made on the available information. The short-term Treasury loans to the Fund are estimated at UAH 5.8 bn.

xcix Information of the Pension Fund / http://www.pfu.gov.ua/pfu/control/uk/publish/article?art_id=162515&cat_id=94750

c The Law of Ukraine, No. 2461-VI, from July 8, 2010

ci According to estimates, the Pension Fund could safe up to UAH 3.5 bn each year due to the increase in retirement age.

cii Initially, the Government planned to reimburse VAT refund arrears proven as of May 1, 2010. Such arrears were estimated at UAH 20 bn.

ciii The Appendix to the Draft State Budget Law for 2011.

civ Spending for debt servicing accounted for 3.7% and 5.1% of central fiscal expenditures in 2008 and 2009, respectively.

cv Law of Ukraine, N 2154-VI from April 27, 2010

cvi Law of Ukraine, N 2154-VI from April 27, 2010 with amendments from July 8, 2010

cvii SPFU Order from September 28, 2010 N 1405

cviii State Budget Law from December 23, 2011

cix President's Order N 1118/2010 from December 10, 2010

Economic Trends		Q3 09	Q4 09	Q1 10	Q2 10	Q3 10	Q4 10	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Industrial production (real)	% yoy cum.	-28.4	-21.9	10.8	12.0	10.8	11.0	12.0	11.1	10.9	10.8	10.7	10.6	11.0
Construction (real)	% yoy cum.	-52.4	-48.2	-21.4	-19.3	-12.6	-5.4	-19.3	-16.7	-14.0	-12.6	-9.0	-8.2	-5.4
Agricultural production (real)	% yoy cum.	3.3	0.1	5.3	3.4	-1.3	-1.0	3.4	-0.6	-4.1	-1.3	-1.2	-1.3	-1.0
Retail trade turnover (real)	% yoy cum.	-16.2	-16.6	-2.6	2.3	5.1	7.6	2.3	4.0	4.6	5.1	5.9	6.8	7.6
Average wage	UAH	1940	2046	1993	2227	2332	2407	2373	2367	2280	2349	2322	2353	2239
CPI	% yoy eop	15.0	12.3	11.0	6.9	10.5	9.1	6.9	6.8	8.3	10.5	10.1	9.2	9.1
PPI	% yoy eop	1.6	14.3	18.6	25.5	19.2	18.7	25.5	24.4	23.3	19.2	19.8	18.9	18.7
Exports (USD)*	% yoy cum.	-43.7	-40.7	22.1	28.9	31.6	…	33.5	33.3	33.2	32.1	29.9	29.8	29.0[e]
Imports (USD)*	% yoy cum.	-49.3	-46.9	18.5	24.7	34.9	…	29.6	30.1	31.8	32.2	33.5	33.9	35.4[e]
Merchandise trade balance	USD bn cum.	-3.7	-5.7	-1.2	-2.0	-4.8	…	-2.5	-3.5	-4.6	-5.4	-6.9	-8.0	-8.4[e]
Current account**	USD bn cum.	-1.1	-1.8	0.0	0.5	-0.3	…	0.5	0.0	-0.6	-0.3	-0.9	-1.4	-2.2
Current account	% GDP, cum.	-1.3	-1.5	-0.7	0.8	-0.3	…	x	x	x	x	x	x	x
Gross international reserves	USD bn eop	28.2	26.5	25.1	29.5	34.7	34.6	29.5	30.9	32.7	34.7	34.3	33.5	34.6
Monetary Base	% yoy eop	7.5	4.4	12.5	16.3	18.0	15.8	16.3	18.3	20.2	18.0	22.8	18.9	15.8
Lending rate on UAH credits	% pa, aop	17.9	19.8	17.4	14.8	13.0	13.6	14.1	13.5	12.6	13.0	13.1	12.8	15.0
Exchange rate (interbank)	USD aop	8.00	8.06	8.00	7.92	7.90	7.96	7.91	7.90	7.89	7.92	7.95	7.95	7.97
Exchange rate (official)	USD aop	7.82	7.99	7.99	7.92	7.90	7.93	7.92	7.90	7.89	7.91	7.91	7.93	7.96
Exchange rate (official)	EUR aop	11.18	11.81	11.07	10.10	10.18	10.79	9.67	10.06	10.18	10.29	10.99	10.87	10.50

Sources: Derzhkomstat, NBU, own calculations
* Monthly figures are only for merchandise exports and imports (source: Derzhkomstat)
Quarterly figures are for trade in goods and services (source: NBU)
** Monthly data are according to the preliminary estimates provided by the NBU
[e] preliminary estimate provided by the NBU

Key Economic Indicators		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Nominal GDP	UAH bn	170.1	204.2	225.8	267.3	345.1	441.5	544.2	720.7	948.1	914.7	1095.0
Nominal GDP	USD bn	31.3	38.0	42.4	50.1	64.9	86.2	107.8	142.7	179.9	117.4	138.0
GDP growth (real)	% yoy	5.9	9.2	5.2	9.6	12.1	2.7	7.3	7.9	2.1	-15.1	4.2
Industrial production	% yoy	13.2	14.2	7.0	15.8	12.5	3.1	6.2	10.2	-3.1	-21.9	11.2
Agricultural production	% yoy	9.8	10.2	1.2	-11.0	19.7	-0.1	0.4	-5.2	17.5	0.1	-1.0
CPI	% yoy aop	28.2	12.0	0.8	5.2	9.0	13.5	9.1	12.8	25.2	15.9	9.4
CPI	% yoy eop	25.8	6.1	-0.6	8.2	12.3	10.3	11.6	16.6	22.3	12.3	9.1
PPI	% yoy aop	20.9	8.6	3.1	7.6	20.5	16.7	9.6	19.5	35.5	6.5	20.9
PPI	% yoy eop	20.8	0.9	5.7	11.1	24.1	9.5	14.1	23.3	23.0	14.3	18.7
Exports (gs, USD)	% yoy	17.9	9.5	10.7	24.0	42.6	7.5	13.2	27.5	33.8	-36.7	27.1
Imports (gs, USD)	% yoy	18.9	14.1	4.9	28.7	31.3	20.4	22.0	35.5	38.6	-43.1	29.3
Current account	USD bn	1.5	1.4	3.1	2.9	6.9	2.5	-1.6	-5.3	-12.9	-1.9	-2.9
Current account	% GDP	4.7	3.7	7.6	5.9	10.6	2.9	-1.5	-3.7	-7.2	-1.7	-1.7
FDI (net)	USD bn	0.6	0.8	0.7	1.4	1.7	6.5	5.3	9.2	9.9	4.5	5.7
International reserves	USD bn	1.5	3.1	4.4	6.9	9.7	19.4	22.4	32.5	31.5	26.5	36.7
Fiscal balance'''	% GDP	-0.7	-1.9	0.8	-0.2	-3.0	-1.9	-0.7	-1.1	-1.5	-2.4	-5.9
Total state debt	% GDP eop	45.3	36.5	33.5	29.0	24.7	17.7	14.8	12.5	19.9	33.0	39.5
External state debt (total)	% GDP eop	33.0	26.3	24.1	21.4	18.6	13.4	11.7	9.8	15.0	21.5	25.3
Monetary base	% yoy eop	39.9	37.4	33.6	30.1	34.1	53.9	17.5	46.0	31.5	4.4	15.8
Exchange rate	USD aop	5.44	5.37	5.33	5.33	5.32	5.12	5.05	5.05	5.27	7.79	7.94
Exchange rate	USD eop	5.44	5.30	5.33	5.33	5.31	5.05	5.05	5.05	7.70	7.98	7.96
Exchange rate	EUR aop	5.03	4.81	5.03	6.02	6.61	6.39	6.34	6.92	7.71	10.87	10.53
Exchange rate	EUR eop	5.10	4.67	5.53	6.66	7.22	5.97	6.65	7.42	10.86	11.68	10.57

Sources: Derzhkomstat, NBU, Ministry of Finance, own calculations
''' "Minus" denotes a consolidated fiscal deficit

Notes:

avg	average
cum.	cumulative
mom	month on month change
qoq	quarter on quarter change
yoy	year on year change
ytd	year-to-date
p.a.	per annum
eop	end of the period
aop	average of the period
gs	goods and services

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INSTITUTE FOR ECONOMIC RESEARCH AND POLICY CONSULTING PRODUCTS

Monthly Economic Monitor Ukraine (MEMU) with supplement

The MEMU contains a monthly review and brief analysis of the key economic policy measures and data that come public during the previous month. The MEMU supplement presents extended analysis of one key event in the Ukrainian economy. There are 12 issues per year disturbed among subscribers.

Macroeconomic Forecast of Ukraine (MEFU)

The MEFU includes forecast of the GDP and its components, fiscal indicators, balance of payments, inflation, exchange rate for current and next years. There are 12 issues per year – 4 quarterly issues and 8 updates with short comments – disturbed among subscribers.

Infrastructure Monitoring of Ukraine (IMU)

The IMU is an annual report that presents information on the restructuring of six key infrastructure sectors of the Ukrainian economy in a standardized manner, which allows for cross-industry comparisons. Monitored indicators are qualitative and fall into three broad categories: (1) commercialisation, (2) tariff reform, and (3) regulatory and institutional development. Twenty-one indicators allow for economic and policy-making analysis at different aggregation levels. It is distributed free of change.

Economic Summary for Ukraine

Economic summary is a review and brief analysis of the key economic indicators and policy measures of the year. It is published in January using the available statistics and annual estimates and updated in May when the most of previous year data becomes publicly available. The product is distributed among subscribers.

Business Tendencies Survey

Business Tendency Surveys are comprised of two surveys. The first one – Industries – is prepared on the basis of quarterly surveys of industrial enterprises managers. The second – Banking – is based on the survey of banks managers. There are four publication for each of the component of the Business Tendencies available and participants of the surveys and to subscribers.

Policy Papers

The policy papers are the joint product of the German Advisory Group for Economic Reforms in Ukraine and the IER aimed at providing economic policy recommendations to Ukraine's policy makers. The recommendations are based on the careful analysis of Ukraine's situation, state-of-the-art economic theory, and best international practices. The papers are available for policy makers and – with some time lag – for general public. The list of the most recent policy papers includes:

- Credit Bureaus in Ukraine: Analysis and Recommendations, by Robert Kirchner, Ricardo Giucci and Vitaliy Kravchuk, Policy Paper 07, December 2010
- Implications of recent developments in global and European natural gas markets for Ukraine, by Georg Zachmann and Dmytro Naumenko, Policy Paper 06, August 2010
- Reforming the Simplified Taxation for Individual Entrepreneurs in Ukraine, by Ricardo Giucci, Robert Kirchner, Oleksandra Betliy and Thomas Otten, Policy Paper 05, August 2010
- Investment Promotion in Ukraine: Blueprint for a Restart, by Alexander Knuth, Ricardo Giucci and Anna Chukhai, Policy Paper 04, August 2010
- Credit Crunch in Ukraine: Facts, Causes and How to Restart Lending, by Ricardo Giucci, Robert Kirchner and Vitaliy Kravchuk, Policy Paper 03, June 2010
- Trade policy in Ukraine: Strategic aspects and next steps to be taken, by Veronika Movchan, Ricardo Giucci and Kateryna Kutsenko, Policy Paper 02, April 2010
- Changing Ukraine's accounting and reporting system: Economic necessity and practical reform steps, by Robert Kirchner, Ricardo Giucci and Thomas Otten, Policy Paper 01, April 2010
- Prospects for Ukraine's steam coal industry – high time for reform, by Lars Handrich, Ferdinand Pavel and Dmytro Naumenko, Policy Paper 09, November 2009
- Official Reserve Adequacy in Ukraine: Assessment and Policy Implications, by Veronika Movchan, Robert Kirchner and Ricardo Giucci Policy Paper 08, November 2009
- Exporting electricity to the EU – more than switching frequencies, by Georg Zachmann and Dmytro Naumenko Policy Paper 07, November 2009
- Current issues of monetary policy in Ukraine by Ricardo Giucci, Robert Kirchner and Vitaliy Kravchuk, Policy Paper 06, November 2009