INSTITUTE FOR ECONOMIC RESEARCH AND POLICY CONSULTING

Monthly Economic Monitor Ukraine

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EXECUTIVE SUMMARY

HIGHLIGHT: REFORM AGENDA

Politics: On November 27, a new Verkhovna Rada was inaugurated. The five pro-European parties, which won the October elections, established a coalition that included a constitutional majority of the members of the Parliament.

Real Sector: Real GDP in the third quarter of 2014 declined by 5.3% yoy due to drop in domestic demand.

Energy sector: At the beginning of December, Ukraine experienced severe power shortages due to a number of factors: shortage of Type A coal at thermal power stations, low water level at hydro power stations and repairs at the Zaporizhzhya nuclear power plant.

Agriculture: The harvested grain volumes are likely to be somewhat higher than last year at near 64 m t.

External sector: Financial and capital account was in deficit at USD 2.8 bn, which was primarily attributed to the repayment on Eurobonds by the Naftogaz at USD 1.6 bn.

Fiscal policy: The Government is unlikely to execute optimistic fiscal revenues plan this year, which envisages increase in revenues by 11%.

Social policy: The Government decided to cease all payments to occupied territories including wages, pensions and social payments to people that live there.

Labour market: Average wage in October dropped by 11.2% yoy in real terms due to financial constraints of companies and high fiscal pressure against the background of accelerated inflation.

Monetary policy: In November, consumer inflation crossed 20% yoy threshold for the first time since February 2009.

Exchange rate: In November, the NBU ceased attempts to keep hryvnia at UAH 13 per USD and as a result hryvnia weakened to UAH 16 per USD.

State debt: In mid-November and early December, the Government received next two tranches in the framework of two EU programs of macro-financial assistance.

Highlight of the month: Reform agenda

FISCAL CONSOLIDATION AS A BASE FOR SUSTAINABLE ECONOMIC DEVELOPMENT

By Oleksandra Betliy, Vitaliy Kravchuk

Economic crisis in Ukraine continues and according to the consensus view real GDP is expected to decline both in 2014 and 2015. Return to economic growth will depend on success of reforms, which were delayed for many years. The broad reform agenda includes changes in all spheres, including defence, security, tax system, energy sector and other infrastructural sectors, healthcare and education. Currently we have already two documents outlining planned reforms: Coalition agreement (CA) and Government program (GP). These documents contain similar (but no identical) measures. Thus, we outline main expected changes in Ukrainian economy.

Sustainable fiscal situation remains top in the agenda. The Government has to continue fiscal consolidation measures taking into account that general government deficit including Naftogaz will exceed 10% of GDP and state debt approaches 70% of GDP this year. In particular, the Government program envisages an ambitious plan to cut general government expenditures by 10% in 2015-2016 (the CA stipulates reduction of fiscal expenditures by 25%). This requires broad set of measures on revenues and expenditures sides.

On the revenues side the Government plans to reduce number of taxes from 22 to 9. Moreover, higher PIT revenues are expected from wage de-shadowing, which is to be stimulated through gradual reduction of single social contribution (payroll tax) from 41% to 15% (or to 23% in the CA) and higher penalties for informal wage payments. At the same time, the impact on wage de-shadowing might be somewhat narrowed due to making PIT rate more progressive. The Government should take into account that wage de-shadowing is likely to take time. As a result, reduction in the single social contribution might result in higher deficit of social security funds, primarily the Pension Fund, what would require higher fiscal transfer. Still, shortage of funds might be counterweighted by higher privatisation receipts for financing central fiscal deficit. In particular, in the nearest future the Government plans to reduce number of companies, which are not subject for the privatisation (from 1500 to 1200 according to the GP and to 500 according to the CA). Higher fiscal revenues are also expected from better VAT administration (though, the approved electronic VAT administration is highly criticized by business) and improved regulation on transferring prices. The GP also suggests special check of all monopolies by the Antimonopoly Committee. It is not clear what is expected from checks (improved competition, lower prices).

In the longer run, economic growth and hence additional fiscal revenues are expected to be ensured by improved investment climate by eliminating unnecessary permits and state control functions and lower corruption. To support SME development, the rate of single tax on small and medium companies is to be halved. Besides, inspections of SMEs will be prohibited. This will create powerful incentive for larger enterprises to become SMEs and withdraw from general taxation but it is unclear whether it will help economic growth.

One of the priorities is regional development and decentralization. The Coalition agreement proposes to channel all capital transfers to regions through the State fund of regional development. Higher decentralization of liabilities and finances is to be ensured. Local government entities are expected to receive more responsibilities (such as environment issues and sport, culture, museums, some social security functions, municipal police), which are to be supported by additional financial resources. In particular, the Coalition agreement envisages that some fraction of EPT and PIT will remain at local level. Additional resources at the local level will come from wider base of property tax including all residential and commercial property, while currently only large residential property is taxed.

Expenditure side measures might be broadly divided to two groups: reduced expenditures and higher efficiency of spending. The Government should start with fiscal transparency and include "recapitalization" spending on bank bailouts and energy subsidies in budget spending and budget deficit. It should also formally recognize that it cannot execute legislatively mandated spending levels on financing of education, healthcare, and agriculture as a certain share of GDP as well as many different subsidies and privileges.

The biggest source of both reduced spending and higher efficiency of spending is the reduction of subsidies to the Naftogaz and replacing it with social spending on direct subsidies to vulnerable households. It will reduce corruption incentives and can lead to higher efficiency social spending.

High recurrent expenditures, particular social payments, will be among the first to be cut. The Government plans to ensure wider means-testing of social assistance and monetize some types of in-kind benefits, which is a long expected step. At the moment, most privileges are provided in-kind to different groups of population (that were instituted in 1990s as a supplement to low monetary wages in budget sector and small social assistance), while coverage by the only means-tested social assistance program – cash assistance to low-income families - remains small due to very strict income eligibility threshold. Recently housing and utility subsidies became more targeted through higher reimbursement rates to poorer households. Changes in social assistance programs are necessary, but they should be complemented by expansion of cash low-income family assistance through increase in income threshold that makes households eligible for the program. In the medium term combining the low-income family assistance and housing and utility subsidy into one social welfare programme for the poor should be considered.

To contain growth of pension liabilities the Government might restrict indexation of pensions in 2015, tax high pensions and change setting of pensions to different groups of employees according to special pension programs. At the same time, the introduction of the second pillar of the pension system, namely accumulative pension system, is to premature taking into account unsustainable financial position of the Pension Fund as well as recent evidence of large losses in accumulative pension fund during financial crisis including in Central European countries.

The Government also plans to reduce size of public sector including through merging of central executive bodies and reduce number of civil servants and public employees. At the moment, there is no clarity on how this process will be undertaken. We believe that the Government should remove overlapping and unnecessary functions from ministries and other state bodies. The idea of combining the Ministry of Social Policy and the Ministry of Healthcare should be studied. The Ministry of Economic Development and Trade should be responsible the deregulation process and investment promotion. Reduction of number of permissions and licences as well as promotion of e-governance will also allow the Government to cut excess labour in state administration.

At the same time, the Government should carefully approach to improving efficiency of spending in healthcare and education including labour cuts. It should be implemented them as part of more comprehensive reforms and focusing more on application “pay for performance” principle for public sector employees.

Besides, expenditures could be saved on reforming the Academy of Science, which remained more or less intact since the Soviet Union times. The Ministries should not have special research institutes, but procure research on open tenders. The healthcare establishments subordinated to different central executive bodies and state-owned companies (such as Ukrzalisnytsia) should be integrated into general healthcare system, which is also in need for reform.

The Coalition agreement and the Government program envisage implementation of healthcare reform. Primary healthcare services are to be expanded, while specialized medical services will be consolidated. Healthcare establishments are to receive higher autonomy, which is required for the increase in efficiency. Principles of healthcare financing are expected to be changed from ‘financing hospital beds’ to ‘financing healthcare provided’, which is an essential change and would result in higher efficiency. The Government also plans to introduce compulsory medical insurance, which, in our opinion, should be delayed until proper healthcare system is functioning.

Another expenditure efficiency measure relates to introduction of electronic public procurement. The procurement system in Ukraine is known for high corruption and overpayments. According to the estimate of Ministry of Justice annual fiscal losses due to non-transparent public procurement amount to UAH 150 bn, which is highly unlikely given that annual spending on goods and services is planned at UAH 128 bn this year but points to significant savings in this area. Therefore, improvement of public procurement, as well as efforts to reduce public sector size might save more money to the Government than petty cuts in social spending.

At the same time, the Government does not pay enough attention to expenditures on economic activity, i.e. state aid. We believe that the Government could use an open political window of opportunity to reform state aid faster than it previously planned. In particular, state aid to coal mining sector should be revised or fully eliminated. This is primarily explained by expected move towards market pricing of coal. State aid to other sectors, i.e. agriculture, should also be thoroughly revised to stop inefficient spending.

To sum up, program documents (CA and GP) envisage number of measures aimed at fiscal consolidation. However, some of them might have opposite effect if implemented very fast all together without preparation and other steps. Besides, important issues remained outside the Government program. Therefore, we would like to hope that these drawbacks will be removed during the preparation of action plan for 2015.

Still, fiscal consolidation and government sector reform is only a first step towards ensuring favourable investment climate and sustainable economic growth. The Government should implement effective anti-corruption measures, prosecution and court reforms. Only comprehensive approach will help Ukraine to return to economic growth.

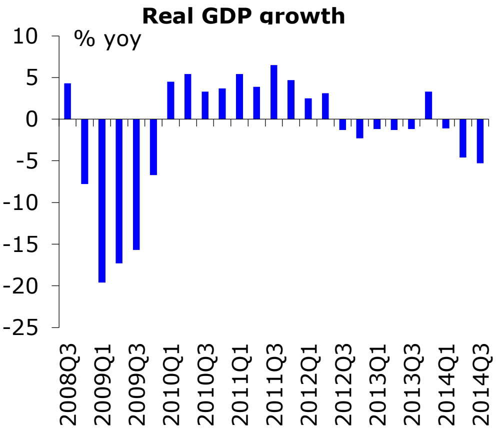
Monthly Economic Monitor Ukraine

Politics: Pro-European coalition formed a semi-technocratic government

Population: 45.5 m
Industry/GDP: 23%
Agriculture/GDP: 10%
Investment/GDP: 18%
Exports to: Russia 24%, EU 26%
Imports from: Russia 30%, EU 35%

The Government. On November 27, a new Verkhovna Rada was inaugurated. The five pro-European parties, which won the October election, established a coalition that included a constitutional majority of the members of the Parliament (302 out of 422 elected MP's). The coalition declared that its main goal was to conduct reforms aimed at resuming economic growth in Ukraine. Reforms are to be based on the Association Agreement between the EU and Ukraine. On December 2, the coalition formed a new government, in which Arseniy Yatsenyuk retained the post of the Prime Minister. Petro Poroshenko Bloc gained 8 out of 20 seats in the Government; the People's Front party got 5 seats (including the one of the Prime Minister); the Samopomich party, the Batkivshchyna party, and the Radical party received 2, 2, and 1 seat(s), respectively (according to the Constitution the Minister for Foreign Affairs and the Minister of Defence are appointed upon request from the President).

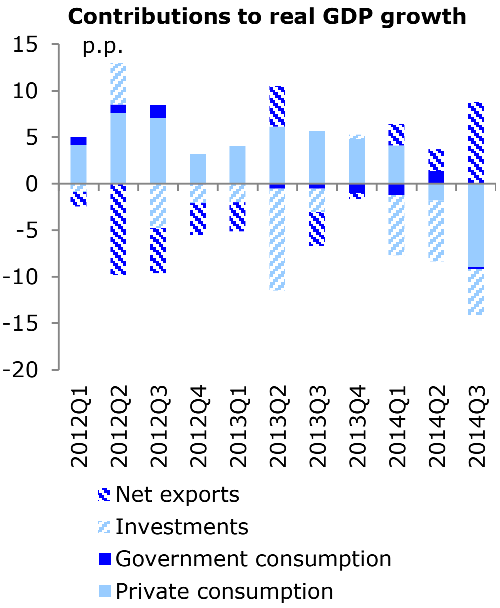
However, the parties gave almost all positions of the ministers responsible for economic policy to professionals that were not politically affiliated, mostly to investment bankers. The professionals got 6 ministerial seats, including the posts of the Minister of Finance, the Minister of Economic Development and Trade, and the Minister of Energy and Coal Industry. Moreover, three out of the six seats were given to foreign nationals. The recruitment of private sector professionals may be seen as a move to facilitate securing foreign financial aid, and boost reforms in order to revive economic growth. On the other hand, it may be also an attempt of the coalition members to shift political responsibility for the unfolding economic crisis. Given the crisis and general political instability, it is likely that the government's lifetime will not be long.



Source: Ukrstat

The war in the East. In November, the low intensity military conflict continued in Donetsk and Luhansk oblasts. Pro-Russian insurgents backed by Russia and Russian troops kept on shelling and attacking Ukrainian troops, but did not succeed to change the front line. According to the United Nations, the death toll of the conflict reached 4,356 as of November 25 (it was 4,035 on October 29, and 3,543 on September, 21, which implies that the average number of casualties in November was roughly the same as in October). The little success of permanent attacks on Ukrainian troops and mounting economic troubles of Russia suggest that the probability of a large-scale war between Russia and Ukraine might decrease. However, the low intensity military conflict is not likely to end in the nearest months.

The IMF. On November 11-25, a technical IMF mission visited Kyiv for the preparation to the second review of Stand-By Arrangement (SBA) with Ukraine. The mission discussed Ukraine's economic policies with top officials. It is expected that the IMF mission visits Ukraine in December. Combined third and fourth tranches of the loan (in the total amount of SDR 1829.3 m that is near USD 2.7 bn) are expected to be provided to Ukraine in January 2015. Earlier it was expected that the disbursements would be made in December.



Source: Ukrstat

Real sector: Sharp decline in consumption

GDP. Real GDP in the third quarter of 2014 contracted by 5.3% yoy (flash Ukrstat estimate was decline by 5.1% yoy). On the demand side, domestic demand dropped sharply. Decline in real disposable income, purchases of foreign currency and net credits repayments by households resulted in drop of real private final consumption at 13.2% yoy. Real gross fixed capital accumulation contracted by 29.9% yoy due to restricted access to financing and cancelled investment plans. Net real exports made positive contribution to economic growth as real exports declined by 19.3% yoy, while real imports dropped by 32.2% yoy.

On the production side, real gross value added in (GVA) dropped in most sectors. Military conflict in the Eastern Ukraine, low domestic and external demand, and trade tensions with Russia resulted in decline of real GVA in manufacturing at 15.2% yoy. Real GVA in construction declined by 26.1% yoy due to restricted financing and hard budget constraints. Lower real private final consumption and industrial output explain decline in real GVA in trade and transport. At the same time, real GVA in agriculture surged by 25.9% yoy primarily due to statistical base effect. Higher spending for defence and security resulted growth of real GVA in state administration and defence by 8.3% yoy.

Sectoral trends. In October the industrial output contracted by 16.3% yoy due to military conflict in the Eastern Ukraine. At the same time, it increased by 7.5% mom as some companies in the region were either able to restart their operation or resumed statistical reporting.

The output in extractive industry contracted by 24.9 yoy. The extraction of coke and lignite dropped by 60.5% yoy as some mines stopped their operation due to military conflict.

Manufacturing declined by 12.4% yoy. In particular, the output in metallurgy decreased by 22.6% yoy, while the manufacture of chemicals dropped by 10.6% yoy).Machine-building production dropped by 26.1% yoy as production of vehicles and locomotives more than halved due to lower demand. At the same time, food production (excluding tobacco and beverages) grew by 7.0% yoy primarily due to earlier processing of sugar beets into sugar.

Retail trade by enterprises dropped by 6.8% yoy between January and October 2014, which reflects decline in real private final consumption.

Construction declined by 31.6% yoy in October due to military conflict in Eastern Ukraine, financial constraints faced by companies and low fiscal capital outlays.

Agricultural production in October decreased by 21.5% yoy due to high statistical base. In particular, the harvesting began later in 2013 because of rains.

Energy: Ukraine is in energy crisis

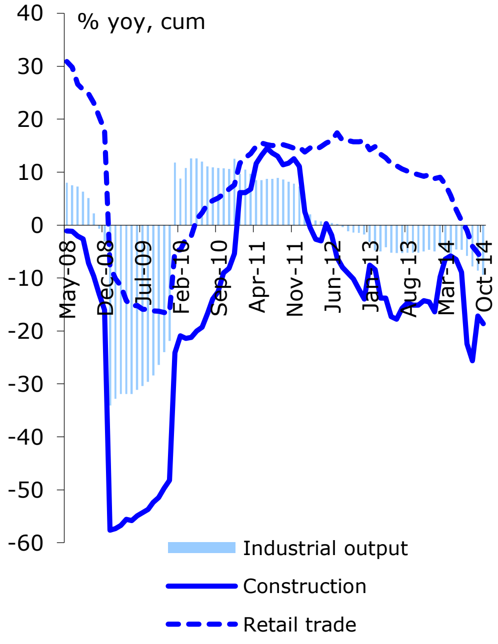
Electricity. At the beginning of December, Ukraine experienced severe power shortages. This happened due to a number of factors: shortage of Type A coal at thermal power stations, low water level at hydro power stations and repairs at the Zaporizhzhya nuclear power plant. As a result, electric power deficit reached 3000-3500 MWt which caused power outages in different regions of Ukraine. As of 10:00 of December 2, Ukraine was consuming 25200 MWt, an increase of 11% yoy. Such increase might be explained by an increase in electricity consumption by households as they use electricity for heating. For January-September 2014, the share of households in electricity consumption increased from 27% to 28.5% while the share of industry decreased from 46.7% to 45.9%. For stable electricity production this winter Ukraine needs to solve problems with coal supply. Otherwise, further power outages are inevitable.

Coal. The Government tries to solve the coal deficit by negotiating coal purchases from Russia, Australia, and South Africa and by transporting coal from Donbas. The latter will become possible after repairing railways near Debaltsevo junction at the East of Ukraine. As of December 2, there were 1.3 m tons of coal at thermal power plants of Ukraine which is three times less than a year before.

Agricultural sector: High grain harvest

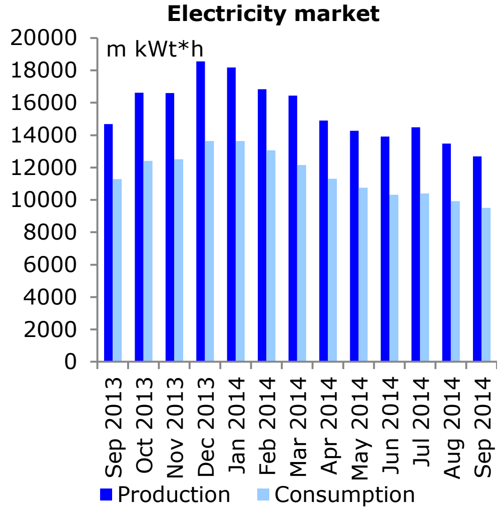
By the end of November, grains and legumes were harvested at the area of 14.5 m ha (98% of sawn area with an average yield of 43.3 quintal per ha. The highest yield at near 60 quintal per ha was reported by Khmelnitska, Vinnytska, Kyivska, Sumska and Cherkaska oblasts. The harvested grain volumes are likely to be somewhat higher than last year at near 64 m t (Crimea and conflict area in the East is not taken into an account). The amount of grain exported or

Real sector trends



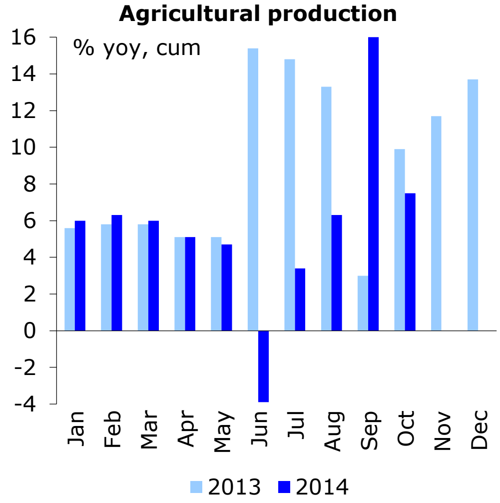
Note: Since April 2014 - data excludes Crimea
Source: Ukrstat

Electricity market



Source: Ministry of Energy

Agricultural production



Source: Ukrstat

already prepared for exports is estimated at about 15 m t including 7 m t of wheat, 3 m t of barley and 4 m t of corn.

External sector: Large financial account deficit because of Eurobond repayments

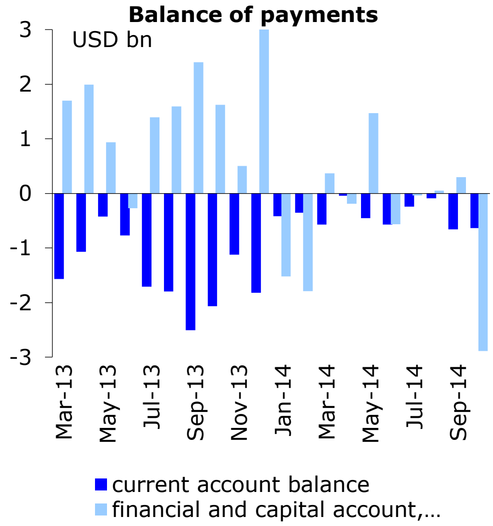
Current account deficit in October remained at USD 0.6 bn. Merchandise trade deficit widened to USD 0.6 bn due to acceleration in exports decline. Services trade was balanced as, on the one hand, lower exports of travel services was compensated by higher exports of telecommunication services, and, on the other hand, imports of travel services continued contracting.

Exports of goods contracted by 24.8% yoy due to military conflict in Donbas and trade tensions with Russia. Minerals exports dropped by 43.1% yoy as coke and ore producers reallocated their sales to domestic market. Restricted access to the Russian market resulted in contraction of machinery exports by 40.4% yoy. Continued contraction of chemicals exports (by 28.3% yoy) was attributed to termination of operation of companies in the occupied territory in the Eastern Ukraine as well as governmental prohibition for fertilizers producers to use domestically produced natural gas till the end of heating period (they should import it on their own).

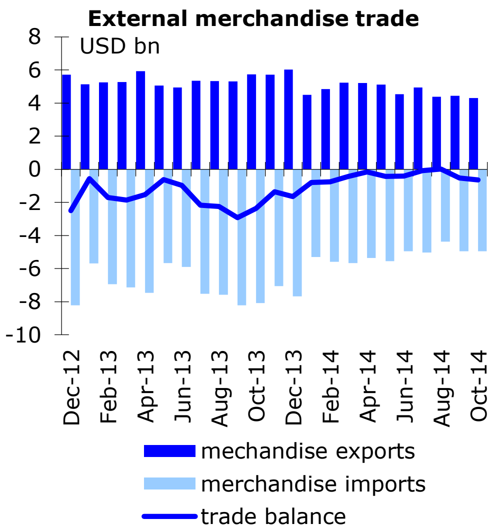
At the same time, exports of food and metals grew each by 2% mom. In particular, food exports gained from autonomous trade preferences by the EU, which mainly affected oil and seeds and meat products, as well as high grains harvest.

In October imports of goods remained at the level of September. Still, it declined by 38.8% yoy due to lower consumption and investment demand and imports substitution explained by hryvnia depreciation. The most affected non-energy groups were food, machinery and wood products. Energy imports dropped by 43.2% yoy, but grew by 10% mom due to imports of natural gas from Norway and coal from South Africa.

Financial and capital account was in deficit at USD 2.8 bn, which was primarily attributed to the repayment on Eurobonds by the Naftogaz at USD 1.6 bn. Outflow of foreign currency from the banking system increased to USD 0.5 bn. At the same time, net inflow of FDI remained weak at USD 0.2 bn.



Source: NBU preliminary estimates



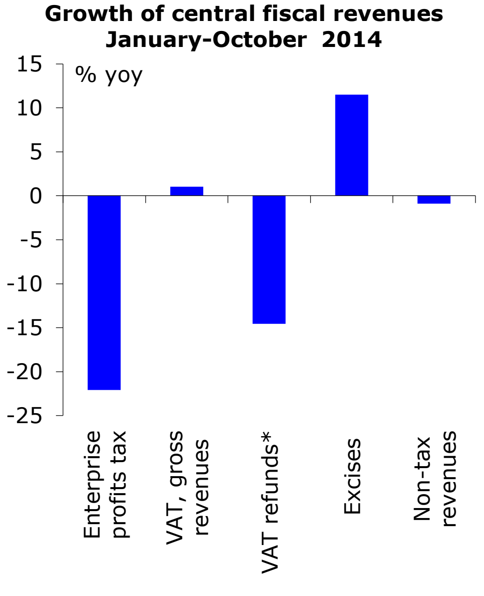
Source: NBU preliminary estimates

Fiscal policy: Fiscal indicators will not be executed fully in 2014

Note: *The State Treasury reported on-going settlement of VAT refund arrears with government bonds as cash refund of VAT. In our opinion this is incorrect (it is more properly accounted for as reduction in payables) and we adjusted data from Treasury reports to exclude the effect of VAT refund arrears settlement on budget revenues.*

Preliminary data. According to preliminary data of the State Treasury between January and November central fiscal revenues (before VAT refund) grew by 5.5% yoy. They grew by more than 10% yoy in November due to introduced military fee, increased rates of excise and rent payments as well as hryvnia depreciation. However, revenues in eleven months of the year were still by 6.8% or UAH 26.7 bn lower than planned. The Government is unlikely to execute optimistic budget plan this year, which envisages increase in revenues by 11%.

10 months. Growth of central fiscal revenues in ten months of 2014 decelerated to 4.6% yoy. Introduction of military fee resulted in growth of PIT revenues due to central budget by 46.3% yoy, but remain lower than planned. Higher excise rates and hryvnia depreciation ensured increased in revenues from excise by 11.5% yoy. At the same time, net VAT revenues (not including VAT refunds by special issue of state domestic bonds) increased by 7.3% yoy due to higher VAT on imports (explained by hryvnia depreciation) and lower VAT refunds. However, EPT revenues dropped by 22.1% yoy due to worse financial results of companies. Non-tax revenues declined by 0.9% yoy after growing by 42% yoy in the first half of year, when the NBU transferred planned amount of its profit to the budget. .



* cash VAT refunds (without VAT-bonds)
Source: State Treasury reports

Lower than planned financing as well as difficulties with procurement particularly in defence and healthcare resulted in under-execution of central fiscal expenditures (general fund) by 6.6% or UAH 20.9 bn. Problems in the Eastern Ukraine resulted in under-execution of state aid to coalmining sector. Capital outlays reached only 33.4% of annual plan.

Central fiscal deficit reached UAH 53.8 bn, but remained lower than planned. It was primarily financed at the expense of external borrowing (IMF loan, the EU and other official donors' assistance). Privatisation receipts remained low due to cancelled privatisation. As a result, the Government revised downwards planned privatisation receipts for 2014 to UAH 0.3 bn from UAH 17 bn.

Social policy: Ceased social payments to the East

East. The Government decided to cease all payments to occupied territories including wages, pensions and social payments to people, that live there. This decision was justified by the diversion of social payment to finance armed groups in the region and the need to pay for free gas and electricity provided to the regions. To receive social assistance people should register in areas under control of Ukraine by December 31. For the reference in 2013 there were 2.1 m pensioners in Donetsk and Luhansk oblasts with annual spending on pensions estimated at UAH 46 bn.

2015. According to recent official announcements the Government plans some cuts in social assistance in 2015. In particular, social assistance is expected to become more means-tested. Some privileges, which are provided to different groups of population, might be eliminated, while some other might be monetised.

Labour market: Real wages declined

Average wage in October grew by only 6.4% yoy in nominal terms. It dropped by 11.2% yoy in real terms due to financial constraints of companies and high fiscal pressure against the background of accelerated inflation. Introduction of military fee also contributed to real wage decline.

Average wage in industry grew by 6.4% yoy, which is slightly above the minimum wage increase (at 6.2% yoy). Nominal average wage in all branches of industry except for extractive industry increased. The most significant growth was in manufacturing of electronic and optical devices (at 19.7% yoy), textile industry (at 17.4% yoy) and publishing (at 12.5% yoy) resulting from an increase in prices and sales quantities. Unexpectedly, average wage in chemical industry also increased by 15.2% yoy: even though many enterprises in the East stopped operating, remaining ones benefited from 33.6% yoy October increase in prices. Wage in extractive industry continued to fall (by 3.0% yoy) as a result of mines closure in the war zone.

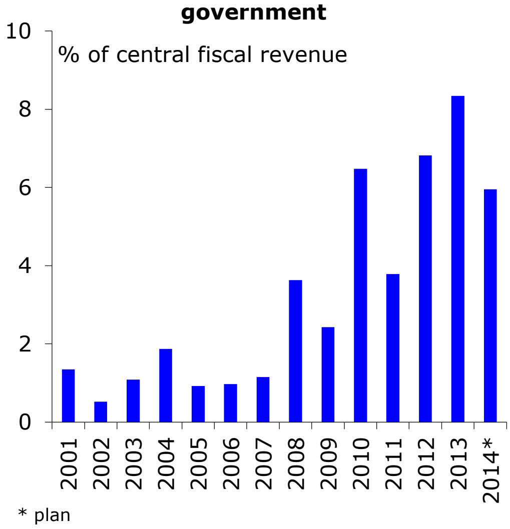
Good harvest of grain and other crops resulted in the increase of nominal wages in agriculture by 7.6% yoy. Fiscal consolidation measures continued to put a downward pressure on wage growth in public sector. For instance, nominal average wage in public administration and defence increased by 2.0% yoy, wage in education and health care grew by 3.4% yoy.

Monetary policy: Inflation reached 21.8% yoy in November

In November consumer inflation crossed 20% yoy threshold for the first time since February 2009. Month-to-month price increase slowed to 1.9% mom as food prices growth decelerated. This is explained by lower fruit and sugar prices and possibly weak consumer demand. However, wide-based price increases continued as hryvnia weakened further relative to dollar in November. Prices for almost all major groups of non-food goods and services increased by 2-3% mom. Due to delayed heating season increase in heating tariffs by 40% approved in May became applicable only in November.

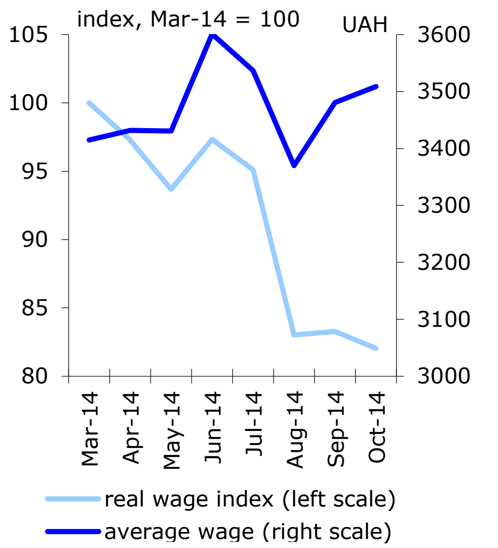
Interbank money market in November remained highly fragmented as some banks borrowed funds from the NBU at 17.5%-20% p.a., while

Transfer of NBU profits to the government



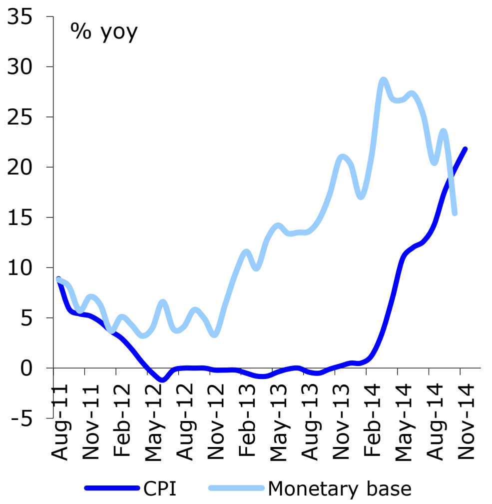
* plan
Source: NBU, State Treasury

Average wage*



*not including AR Crimea
Source: Ukrstat

CPI and monetary base development



Source: Ukrstat, NBU

others on interbank market at average interest rate of 14-16% p.a. At the same time, a number of banks park large amounts of spare liquidity at the NBU overnight for 7.5% p.a. This points to low confidence between banks. Still, overall amounts of liquidity in banking sector remained large and double-digit interest rates reflected NBU monetary policy and high inflation expectations.

Exchange rate: New weakness of hryvnia

In November the NBU ceased attempts to keep hryvnia at UAH 13 per USD and as a result hryvnia weakened to UAH 16 per USD and later fluctuated in UAH 15-16 per USD range. However depreciation expectation remains, what hampers functioning of the interbank market. New depreciation of hryvnia is more than sufficient to balance trade flows, but situation with financial account transactions remains difficult.

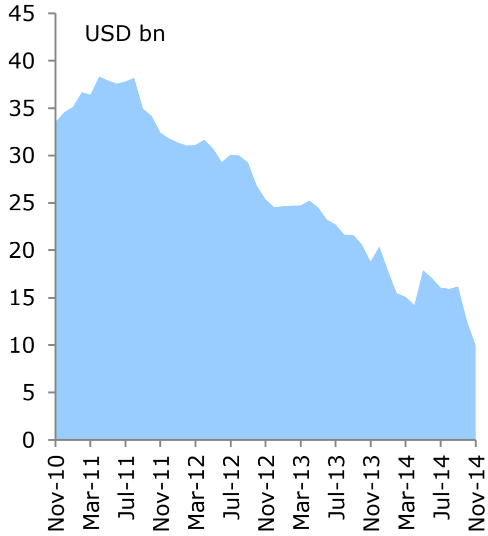
NBU international reserves continued to drop at spectacular pace as they reached USD 9.9 bn in November as compared to USD 16.4 bn in September. This reflected high payments on foreign currency debt and transfers to the Naftogaz, while external borrowing was minimal in October and November.

State debt: Next tranches of external financial aid received

Domestic debt. In November the Ministry of Finance placed UAH 7.1 bn of hryvnia denominated bonds with weighted average yield at 16.4% on primary market. Five- and ten-year bonds accounted for 67.0% of the total placement. Besides, the Government issued UAH 7.5 bn of ten-year state domestic bonds (out of USD 10.1 bn earlier approved by the Cabinet of Ministers) directed for the financial support to the Deposit Guarantee Fund.

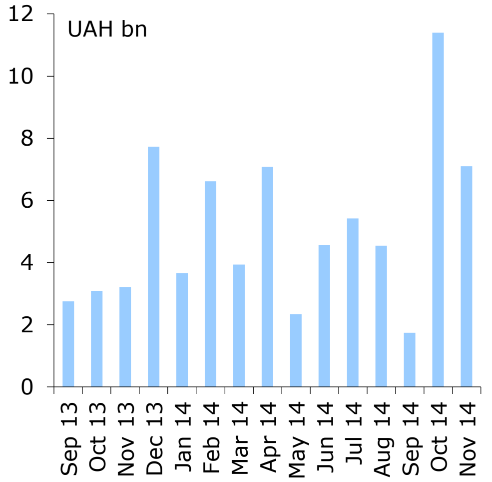
External debt. In mid-November and early December, the Government received next two tranches in the framework of two EU programs of macro-financial assistance (EUR 260 m out and EUR 500 m, respectively). The loans were granted with ten- and fifteen-year maturity correspondingly. As of December 1, 2014 Ukraine has received in total EUR 1.36 bn within these programs (out of EUR 1.61 bn). The financial support is aimed at supporting structural reforms to ensure sustainable economic growth and sound financial situation. The last MFA tranche of EUR 250 m is expected in February 2015. It is conditional upon the IMF Program implementation results.

NBU international reserves



Source: NBU

State domestic bonds placements in UAH (without recapitalisation)



Source: NBU

Tables

Economic Trends		Q3 12	Q4 12	Q1 13	Q2 13	Q3 13	Q4 13	Q1 14	Q2 14	Q3 14	Dec	Jan	Feb	Mar	Apr[c]	May[c]	Jun[c]	Jul[c]	Aug[c]	Sep[c]	Oct[c]	Nov[c]
Industrial production (real)	% yoy cum.	-1.2	-1.8	-5.0	-5.3	-5.2	-4.7	-5.0	-4.7	-5.8	-4.7	-5.0	-4.2	-5.0	-5.3	-4.6	-4.7	-5.8	-7.8	-8.6	-9.4	…
Construction (real)	% yoy cum.	-9.1	-14	-13.8	-17.8	-15.1	-14.5	-6.4	-8.9	-22	-14.5	-16.4	-9.8	-6.4	-5.8	-6.5	-8.9	-22.4	-4.0	-17.2	-18.6	…
Agricultural production (real)	% yoy cum.	-4.6	-4.5	5.8	15.4	3.0	13.7	6.0	-3.9	3.4	13.7	6.0	6.3	6.0	5.0	4.7	-3.9	3.4	6.3	16.0	7.5	…
Retail trade turnover (real)	% yoy cum.	16.0	15.9	13.4	11.2	9.8	9.5	7.7	0.8	-1	9.5	8.8	9.0	7.7	5.6	2.9	0.8	-1.0	-4.0	-5.3	-6.8	…
Average wage	UAH	3064	3195	3085	3289	3331	3390	3245	3488	3549	3619	3148	3189	3398	3432	3430	3601	3537	3370	3739	3754	…
CPI	% yoy eop	0.0	-0.2	-0.8	-0.1	-0.5	0.5	3.4	12.0	12.6	0.5	0.5	1.2	3.4	6.9	10.9	12.0	12.6	14.2	17.5	19.8	21.8
PPI	% yoy eop	0.3	0.3	0.2	-1.6	-0.9	1.7	3.9	15.9	22.5	1.7	1.9	3.3	3.9	6.1	8.8	15.9	22.5	24.2	26.9	25.9	32.8
Exports (USD)*	% yoy cum.	2.6	1.0	-4.7	-7.1	-6.2	-5.2	-7.7	-6.5	-13.9	-7.6	-12.2	-10.0	-6.8	-8.3	-6.4	-6.7	-6.8	-8.2	-9.1	-10.8	…
Imports (USD)*	% yoy cum.	7.6	5.6	-0.8	-8.3	-4.1	-3.4	-14.7	-18.6	-38.5	-5.8	-6.7	-13.6	-16.1	-19.9	-17.3	-17.3	-19.5	-22.4	-24.8	-26.3	…
Merchandise trade balance	USD bn cum.	-14.8	-20.5	-4.0	-7.1	-14.2	-19.6	-1.9	-0.6	-0.6	-19.6	-0.8	-1.5	-1.9	-2.0	-2.2	-2.5	-2.7	-3.0	-3.6	-4.2	…
Current account**	USD bn cum.	-10.0	-14.4	-3.1	-5.5	-11.4	-16.4	-1.3	-0.6	-1.0	-16.1	-0.4	-0.8	-1.3	-1.2	-1.5	-1.9	-2.3	-2.7	-3.3	-4.0	…
Gross international reserves	USD bn eop	29.3	24.5	24.7	23.2	21.6	20.4	15.1	17.1	16.4	20.4	17.8	15.5	15.1	14.2	17.9	17.1	16.1	15.9	16.4	12.6	10.0
Monetary Base	% yoy eop	5.8	6.4	9.9	13.4	14.8	20.3	28.5	25.1	23.5	20.3	17.0	21.0	28.5	26.8	26.7	27.3	25.1	20.4	23.5	15.4	13.8
Lending rate on UAH credits	% pa, aop	19.6	20.8	16.2	15.4	15.3	16.5	18.5	17.5	16.4	17.4	15.1	20.3	20.0	17.5	17.9	17.2	16.1	16.8	16.2	16.3	16.7
Exchange rate (interbank)	USD aop	8.10	8.15	8.12	8.14	8.15	8.21	9.1	11.71	12.6	8.24	8.37	9.08	9.98	11.61	11.78	11.79	11.74	12.98	13.01	12.93	14.75
Exchange rate (official)	USD aop	7.99	7.99	7.99	7.99	7.99	7.99	8.9	12.71	12.6	7.99	7.99	8.65	9.92	11.64	11.64	11.81	11.76	12.95	13.02	12.95	14.70
Exchange rate (official)	EUR aop	9.99	10.37	10.55	10.44	10.58	10.87	12.14	13.71	16.67	10.94	10.92	11.80	13.69	16.08	16.00	16.04	15.93	17.25	16.83	16.43	18.36

Sources: Ukrstat, NBU, ICAP, own calculations

* Monthly figures are only for merchandise exports and imports (source: NBU, preliminary data)
Quarterly figures are for trade in goods and services (source: NBU)

** Monthly data are according to the preliminary estimates provided by the NBU

[c] Data excludes Crimea

Key Economic Indicators		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Nominal GDP	UAH bn	170.1	204.2	225.8	267.3	345.1	441.5	544.2	720.7	948.1	913.3	1082.6	1302.1	1408.9	1454.9
Nominal GDP	USD bn	31.3	38.0	42.4	50.1	64.9	86.2	107.8	142.7	179.9	117.2	136.4	163.4	176.3	182.0
GDP growth (real)	% yoy	5.9	9.2	5.2	9.6	12.1	2.7	7.3	7.9	2.3	-14.8	4.1	5.2	0.3	0.0
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	7.3	-0.5	-4.7
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	17.5	-4.5	13.7
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	8.0	0.6	-0.3
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	4.6	-0.2	0.5
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	19.0	3.7	-0.1
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	14.2	0.3	1.7
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	28.2	1.0	-5.2
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	33.8	5.6	-3.4
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	-9.3	-14.3	-16.4
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	-5.7	-8.1	-9.0
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	6.6	6.6	3.4
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	31.8	31.4	20.4
Fiscal balance'''	% GDP	-0.7	-1.9	0.8	-0.2	-3.0	-1.9	-0.7	-1.1	-1.5	-2.4	-6.0	-1.8	-3.6	-4.4
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	39.9	36.0	37.4	40.1
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	25.6	22.8	22.0	20.6
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	6.3	6.4	20.3
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	7.97	7.99	7.99
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	7.99	7.99	7.99
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	11.09	10.27	10.61
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	10.54	10.30	11.04

Sources: Ukrstat, NBU, Ministry of Finance, own calculations

''' "Minus" denotes a consolidated fiscal deficit; without recapitalisation

Notes:

avg	average	**ytd**	year-to-date	**NBU**	National Bank of Ukraine
cum	cumulative	**p.a.**	per annum	**EPT**	Enterprise profit tax
mom	month on month change	**eop**	end of the period	**VAT**	Value added tax
qoq	quarter on quarter change	**aop**	average of the period	**Ukrstat**	State Statistics Service of Ukraine
yoy	year-on-year change	**gs**	goods and services		

Quarterly trends

National accounts		Q4 09	Q1 10	Q2 10	Q1 11	Q2 11	Q3 11	Q4 11	Q1 12	Q2 12	Q3 12	Q4 12	Q1 13	Q2 13	Q3 13	Q4 13	Q1 14	Q2 14[c]	Q3 14[c]
GDP	UAH bn	259.9	217.3	256.8	257.7	311.0	369.8	363.6	293.5	349.2	387.6	378.6	302.9	353.0	394.7	404.3	313.0	372.7	428.2
GDP (real)	% yoy	-6.7	4.5	5.4	5.1	3.9	6.5	5.0	2.5	3.1	–1.3	-2.3	-1.2	-1.3	-1.2	3.3	-1.1	-4.6	-5.3
Household consumption (real)	% yoy	-16.2	0.2	6.8	13.2	14.2	16.1	18.5	7.8	12.3	11.0	5.5	6.5	9.5	8.4	6.8	5.7	-2.3	-13.2
State consumption (real)	% yoy	-3.7	3.8	-4.0	2.0	2.9	-9.4	-6.6	3.3	4.8	9.9	1.5	1.1	-2.3	-3.3	-2.5	-9.1	6.9	-0.8
Gross fixed capital formation (real)	% yoy	-33.7	-5.7	-3.2	-1.8	3.7	9.7	12.0	13.8	17.5	-5.2	-4.9	7.0	-17.4	-7.7	-5.1	-19.1	-18.5	-29.9
Exports of goods and services (real)	% yoy	6.9	0.4	13.2	19.4	4.9	0.3	-4.1	-7.3	-8.1	-3.8	-9.6	-9.0	-14.3	-7.9	-4.1	-2.0	-7.4	-19.3
Imports of goods and services (real)	% yoy	-11.1	-6.2	17.2	38.1	23.3	12.5	5.2	-3.0	9.0	4.3	-2.6	-2.4	-18.4	-0.7	-1.8	-7.0	-11.3	-32.2
Agriculture, hunting, forestry (real)*	% yoy	-11.6	5.4	0.5	4.9	1.3	16.7	38.1	0.5	11.5	-8.3	-4.0	5.7	20.8	-2.0	38.2	6.0	-8.8	25.9
Manufacturing industry (real)*	% yoy	6.5	10.9	10.1	7.8	3.4	4.6	-2.9	1.1	1.8	-4.8	-5.5	-9.5	-9.2	-9.8	-8.9	-6.8	-8.4	-15.2
Construction (real)*	% yoy	-32.8	-7.7	-5.8	1.7	10.9	0.1	2.0	1.2	3.4	-15.3	-20.8	-14.9	-20.8	-11.1	-7.7	-3.9	-16.9	-26.1
Trade, repair services (real)*	% yoy	-16.4	6.1	9.6	9.8	2.8	6.1	3.0	3.2	4.6	0.4	-1.2	1.6	-0.2	1.9	4.7	3.1	-9.1	-17.8
Transport (real)*	% yoy	-0.4	1.3	1.8	10.2	7.9	5.7	11.1	-2.3	-3.3	-8.4	-9.5	-2.7	-0.6	2.8	2.8	-5.8	-6.1	-7.1
Balance of payments																			
Current account balance	USD bn	-0.9	0.0	0.5	-1.6	-1.7	-2.6	-4.4	-2.1	-3.8	-4.0	-4.9	-3.1	-2.3	-6.0	-4.9	-1.3	-0.6	-1.0
Current account balance	% of GDP	-2.7	-0.1	1.6	-4.9	-4.4	-5.6	-9.5	-5.6	-8.7	-8.3	-10.3	-8.3	-5.1	-12.2	-9.8	-3.8	-2.1	-2.9
Trade balance in goods	USD m	-1407	-1236	-697	-3597	-2851	-4580	-5224	-3867	-5577	-5215	-5833	-4045	-3053	-7232	-5268	-1949	-567	-585
Trade balance in services	USD m	550	930	1115	1262	1514	2007	1312	1299	1362	1975	1084	822	893	1919	480	589	142	-325
Current transfers	USD m	722	608	728	1039	878	988	803	683	805	777	711	533	589	480	547	232	472	284
Direct investment (FDI)	USD m	1282	923	1196	880	2422	2090	1623	1663	1091	2002	1871	821	472	1199	859	-713	-292	606
Portfolio investments (equity)	USD m	41	-20	-18	149	113	42	207	-3	74	83	339	705	579	664	-757	-239	-53	-77
Gross international reserves	USD bn	26.5	25.1	29.5	36.4	37.6	35.0	31.8	31.1	29.3	29.3	24.5	24.7	23.2	21.6	20.4	15.1	17.1	16.4
Exchange rate (interbank), UAH/USD	aop	8.06	8.00	7.91	7.95	7.98	7.99	8.01	8.03	8.04	8.09	8.11	8.11	8.14	8.15	8.21	9.14	11.71	12.58
Exchange rate (official), UAH/USD	aop	7.99	7.99	7.91	7.94	7.97	7.97	7.98	7.99	7.99	7.99	7.99	7.99	7.99	7.99	7.99	8.86	12.71	12.58
Fiscal indicators																			
Consolidated fiscal revenues	% of GDP	36.0	30.9	30.4	32.8	30.0	29.5	30.7	33.6	31.6	28.2	33.7	35.3	29.5	29.1	28.9	35.8	30.1	29.2
Personal income tax	% of GDP	4.7	4.9	4.8	5.0	4.8	4.2	4.7	5.1	4.9	4.4	5.0	5.3	5.1	4.7	4.9	5.2	4.8	5.0
Enterprise profits tax	% of GDP	3.6	4.3	3.0	4.5	4.5	3.6	4.4	4.9	4.1	2.9	4.2	6.2	3.4	3.0	3.0	5.0	2.5	2.2
Value-added tax	% of GDP	11.0	9.8	9.8	7.6	12.9	9.6	9.6	10.8	10.3	8.6	10.0	9.7	9.1	8.2	8.5	8.8	9.7	8.1
Excise tax	% of GDP	2.6	2.4	3.0	2.1	3.0	2.7	2.4	2.8	2.9	2.8	2.4	3.1	2.6	2.3	2.2	2.5	3.0	3.6
Consolidated fiscal expenditures	% of GDP	34.5	33.0	38.7	32.8	33.1	26.9	35.6	33.7	33.8	30.7	41.4	37.0	36.0	30.4	36.3	35.7	35.6	32.2
Current expenditures	% of GDP	31.4	32.4	37.4	31.5	30.8	23.9	30.1	31.8	31.3	27.7	37.4	35.7	34.1	28.5	33.5	35.2	34.6	30.5
Capital expenditures	% of GDP	3.1	0.6	1.4	1.3	2.4	3.0	5.5	1.9	2.4	2.9	4.0	1.3	1.9	1.9	2.8	0.5	1.0	1.7
Consolidated fiscal balance	% of GDP	1.1	-2.0	-8.0	-0.3	-3.4	-3.9	-5.5	-0.2	-2.6	-3.0	-7.8	-1.9	-6.3	-1.5	-7.4	0.1	-5.5	-3.3
Privatisation receipts	% of GDP	0.0	0.1	0.0	0.4	3.2	0.0	0.1	1.4	0.3	0.1	0.4	0.0	0.0	0.2	0.1	0.0	0.0	0.0
Labour market																			
Average wage (real)	% yoy	-5.7	3.3	8.7	11.1	5.5	7.7	10.8	14.7	16.5	13.3	12.9	9.9	9.3	8.1	5.9	3.5	-4.1	-10.9
Household income (real)	% yoy	-7.6	3.7	11.8	7.8	1.9	7.3	7.7	6.0	13.0	10.4	9.4	8.9	5.7	2.5	4.7	1.9	-1.9	…
Unemployment rate (ILO methodology)	% cum	9.4	9.0	7.9	8.7	7.7	6.9	8.2	8.4	7.1	6.6	8.0	8.0	7.5	7.0	7.6	8.8	8.2	…
Banking system																			
Monetary aggregate M0	% yoy cum	1.5	5.4	9.9	15.7	11.5	8.6	6.3	4.7	6.7	5.2	5.5	9.7	9.8	12.3	17.0	19.2	31.9	28.8
Monetary aggregate M2	% yoy cum	-5.4	6.9	13.2	25.5	22.0	16.0	14.4	11.2	9.0	10.7	13.1	16.0	17.9	19.2	17.5	17.7	13.4	23.8
Household deposits in national currency	% yoy cum	-8.5	7.1	20.1	43.3	26.0	16.7	12.3	14.4	16.4	16.3	16.3	19.1	26.5	33.4	38.0	7.9	-2.3	-12.3
Household deposits in foreign currency	% yoy cum	4.7	22.8	21.5	19.7	21.0	15.7	13.4	12.4	10.8	17.0	21.8	17.0	14.7	8.4	0.9	19.8	10.2	5.5
Com. bank credits in national currency	% yoy cum	16.9	13.6	8.3	16.0	18.5	21.1	21.0	17.4	15.3	9.1	7.7	8.6	7.4	10.2	16.9	12.3	4.9	-0.8
Com. bank credits in foreign currency	% yoy cum	-15.2	-13.7	-10.5	-2.1	0.9	-2.3	-4.2	-7.0	-10.8	-9.9	-7.3	-4.4	-0.4	0.8	2.8	36.4	38.5	49.1
Long-term com. bank credits	% yoy cum	-3.8	-3.9	-2.8	5.0	6.3	5.3	2.9	-2.9	-7.0	-8.0	-6.6	-5.6	-2.7	-0.5	2.9	26.3	24.4	24.6
Long-term com. bank credits	% of total	68.1	68.5	68.9	67.2	66.6	64.4	62.9	61.5	59.8	59.1	57.8	55.9	55.7	55.1	53.2	58.5	59.1	59.8
Average lending rate on national currency credits	% p.a.	19.8	17.3	15.0	13.1	13.5	14.1	18.4	15.5	15.6	19.5	20.8	16.2	15.3	15.3	16.5	18.4	17.5	16.4
Average lending rate on foreign currency credits	% p.a.	10.1	10.9	11.1	10.2	9.8	8.8	8.4	8.2	8.2	8.5	8.8	9.4	9.7	9.6	8.8	8.7	9.4	9.2

Sources: National Bank of Ukraine, State Committee of Statistics, State Treasury, Ministry of Finance, Reuters, IER estimates
* change in value added
[c] Data excludes Crimea, preliminary NBU estimates for balance of paymer

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