

May 2018

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Executive Summary

- ❖ During May 2018, Russian-backed separatists continued their attacks against Ukrainian troops and civilians on the border areas of the occupied territories. The average daily number of attacks against Ukraine is around 25.
- ❖ After weeks of negotiations, Verhovna Rada enacted the Anticorruption Court Law in early June. Seventy percent of the Ukrainian parliamentarians voted in favor of the Law. However, it is not yet clear if this law will be consistent with the recommendations of the Venice Commission. The IMF is studying the wording of the law as it is feared that there may be deficiencies. If this were to be the case, amendments will need to be introduced.
- ❖ In April 2018, the Ukrainian economy continued its recovery. In fact, industrial production increased by 3% on a year-over-year basis. This improvement was supported by good performance in mining and quarrying, with mining of coal and lignite increasing by 13.2 % yoy, mining of metal ores by 9% yoy, and quarrying by 5.6% yoy. Manufacturing increased by 0.8% yoy in April, compared to a decline of -4.6% yoy in March.
- ❖ Fiscal budget performance continues to be satisfactory. The consolidated fiscal budget of Ukraine was executed with a surplus of UAH 3.0 billion in April. The UAH 3.0 billion surplus was generated solely by local budgets as the state budget was virtually balanced.
- ❖ Consumer inflation saw little changes in April. The all items index declined by 0.1 percentage point to 13.1% yoy. Continued supply-driven growth in foodstuff prices remained the major driver of inflation.
- ❖ In the banking sector, the growth of hryvnia deposits accelerated to 14.7% yoy in April thanks to more than doubled growth in corporate sector deposits. On the other hand, foreign currency deposits denominated in USD sustained a decline of 0.9%, leading to a reverse of its growth trend. The situation with bank lending activities further improved in April. National currency loans expanded at a rate of 15.7% yoy, while foreign currency loans denominated in USD saw their rate of decline decelerating to 0.6% yoy.
- ❖ The UAH/USD exchange rate remained stable in May, ending the month at around 26.1 UAH/USD.
- ❖ In April 2018, Ukraine's current account of the balance of payments achieved a surplus of USD 175 million, compared to a deficit of USD 628 million in March. Such improvement was caused by a surplus in the primary income account of USD 308 million, a surplus of USD 252 million in the secondary income account, and a reduction in the deficit of the merchandise and services trade account to USD -385 million. The current account surplus and financial account inflows of USD 119 million in April led to an increase in international reserves to USD 18.4 billion.

Main Macroeconomic Indicators	2012	2013	2014	2015	2016	2017	2018f
GDP, USD billion	173	180	130	87	93.4	104	113
Real GDP Growth, % yoy	0.2	0.0	-6.6	-9.9	2.3	2.5	3.0
Fiscal Balance (incl. Naftogaz/Pension Fund), % of GDP	-5.5	-6.5	-11.7	-2.1	-2.3	-1.5	-2.5
Public Debt, External and Domestic, % of GDP	36.6	40.4	69.4	79.1	81.2	78.5	78.0
Consumer Inflation, eop, % yoy	-0.2	0.5	24.9	43.3	12.4	13.7	9.0
NBU Key Policy Interest Rate, % eop	7.5	6.5	14.5	17.0	16.7	16.4	17.0
Hryvnia Exchange Rate per USD, eop	8.1	8.2	15.8	24.0	27.1	28.1	28.0
Current Account Balance, % of GDP	-8.3	-9.2	-3.5	-0.2	-3.8	-3.7	-3.5
Merchandise Exports, USD billions	64	59	51	35	34	40	43
Merchandise Imports, USD billions	86	81	58	39	40	49	52
FDI, Net Annual Inflow, USD billion	8.4	4.5	0.4	3.0	3.3	2.3	5.0
International Reserves, USD billion	24.5	20.4	7.5	13.3	15.5	18.8	21.0
Public External Debt, USD billion	32.1	31.7	34.9	42.6	42.5	47.0	52.0
Private External Debt, USD billion	102.3	110.3	91.2	76.0	69.9	67.0	72.0

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Political and Reform Developments

During May 2018, Russian-backed separatists continued their attacks against Ukrainian troops and civilians located on the border areas with the temporarily occupied territories. The average daily number of attacks against Ukraine is around 25. Their intensity varies with the time of the day, with the most intensive attacks concentrated in the night. At the end of May, two Ukrainian civilians were killed by terrorists, including one 14-year old teenager girl in a small village Zaliznoye. Since the beginning of the conflict in 2014 the total number of casualties among civilians and militants exceeded 10,000.

In May, the security situation in Ukraine was discussed in a meeting of the UN Security Council. Representatives of the USA and EU and the Ukrainian Minister of Foreign Affairs Pavlo Klimkin made strong calls to Russia to resolve the conflict. The Ukrainian security issue is also in the agenda of the NATO meeting in Brussels, which is scheduled for June. The meeting will be attended by a Ukrainian high level delegation led by the Minister of Defense Stepan Poltorak. It was also announced that a meeting of Foreign Ministers under the Normandy format group (Germany, France, Ukraine and Russia) is scheduled for mid-June to discuss the security situation in Donbas and the need to introduce the UN peacekeeping mission as soon as possible.

After weeks of negotiations, Verhovna Rada enacted the Anticorruption Court Law in early June. Seventy percent of the Ukrainian parliamentarians voted in favor of the Law. However, it is not yet clear if this law will be consistent with the recommendations of the Venice Commission. The IMF is studying the wording of the law as it is feared that there may be deficiencies. If this were to be the case, some amendments will need to be introduced to the law. After the correction of deficiencies, the effective implementation of the Anticorruption Court Law should start a new era in Ukraine's fight against corruption. It should positively affect the quality of the investment climate in the country. It is also an important element to unblock Ukraine's access to the funds of international financial institutions including the IMF, EC and World Bank.

On June 7, Verhovna Rada accepted the resignation of the Minister of Finance from his position. This was due to conflicts between the Prime Minister and the Minister of Finance. The Acting Minister will be Deputy Minister Oksana Markarova, who started her career in the public sector right after the Dignity Revolution as a first deputy of the former Minister Natalie Jaresko. The appointment of Ms. Markarova is not expected to affect country's relations with any of the international institution since she has been deeply involved into the management of the ministry for several years and has pledged to continue the reform agenda of the ministry.

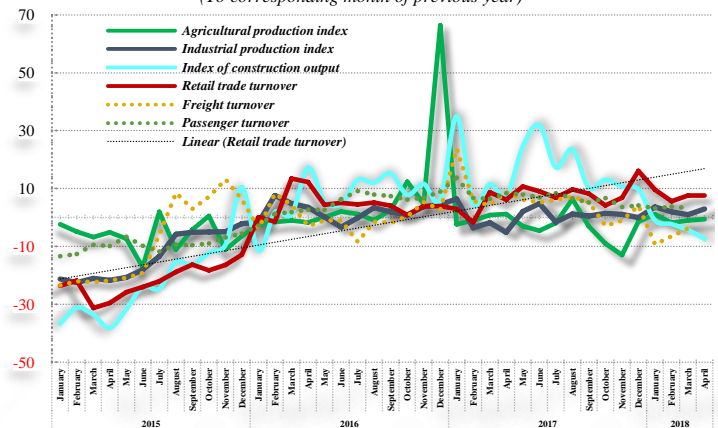
Economic Growth

During the first quarter of 2018, Ukrainian real GDP continued its recovery, growing by 3.1% yoy, compared to 2.8% yoy in the first quarter of 2017.

High-frequency data for April 2018 also confirmed Ukraine's recovery. In April 2018, industrial production increased by 3%, on a year-over-year basis. The above-mentioned improvements of industrial output were supported by good performance in mining and quarrying, with mining of coal & lignite increasing by 13.2 % yoy, mining of metal ores by 9% yoy, and quarrying by 5.6% yoy.

Ukraine Economic Performance by Sector, % yoy

(To corresponding month of previous year)



Source: State Statistics Committee, the Bleyzer Foundation

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In April 2018, manufacturing output increased by 0.8% yoy, compared to a decline of -4.6% yoy in March. The largest expansion in manufacturing production took place in the following subsectors: chemical products (31.1% yoy), coke & refined petroleum products (19.3% yoy), electricity, gas, steam & air conditioning supply (8.6% yoy), engineering (5.2% yoy), and wood products (4.9% yoy). However, negative results took place in the extraction of crude petroleum and natural gas (-1.6% yoy), plastic production (-6.3% yoy), foodstuffs (-4.1% yoy) and pharmaceutical products (-2.4% yoy). In terms of the main industrial groups, the major increases took place in investment goods (with a growth of 7.5% yoy), energy goods (7.8% yoy), intermediate consumption goods (2.2% yoy) and consumer durables (1.8% yoy).

Ukraine's recovery was supported by higher income growth of the populations (12.5% yoy in real terms). These increases permitted Ukrainian retail trade turnover to maintain a high growth of 7.6% yoy in April 2018. On the other hand, the agricultural sector of Ukraine continued to show negative results, with an output decline of -0.6% yoy in April 2018. In similar manner, Ukrainian construction output in April also declined by -7.4% yoy, compared to -4.3% yoy drops in March 2018. Cargo transportation shrunk by -2.8% yoy, while passenger transportation grew by 1.2% yoy in January-April 2018 (with aircraft transportation growing by 18.2% yoy).

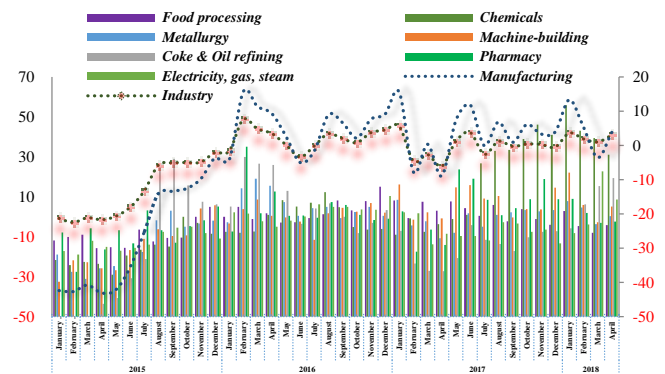
Regarding industrial production growth in the regions, the largest expansions took place in the following oblasts: Ivano-Frankivsk (14.8% yoy), Donetsk (11.5% yoy), Volyn (8.3% yoy), Poltava (8% yoy), Dnipropetrovsk (6.9% yoy), Sumy (6.4% yoy), Kirovohrad (6.3% yoy), Cherkasy (6.1% yoy), Chernivtsi (6.1% yoy), Ternopil (5% yoy).

On the other hand, in April 2018, nine regions of Ukraine had reductions in production, with the highest drops in Rivne (-23% yoy), Khmelnytskyi (-20% yoy), Vinnytsya (-12% yoy), Chernihiv (-10% yoy), Kharkiv (-9.3% yoy), Zhytomyr (-5.5% yoy), Kyiv city (-4.5% yoy), Odesa (-3.1% yoy), Mikolayiv (-2% yoy).

Fiscal Policy

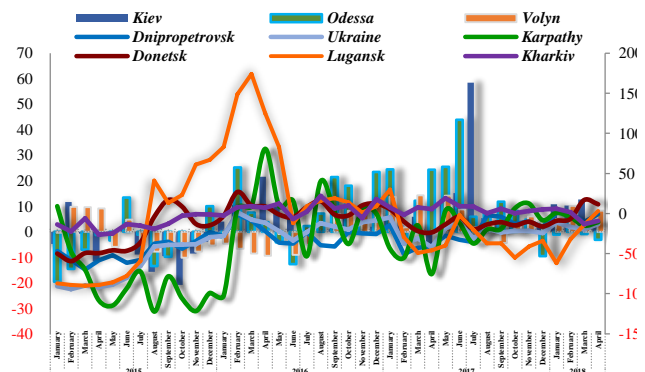
The consolidated fiscal budget of Ukraine was executed with a surplus in April. The UAH 3.0 billion surplus was generated solely by local budgets as the state budget was virtually balanced. The April budget surplus fully covered the cumulative consolidated budget deficit of Q1, meaning that the consolidated budget balance was close to zero in January-April. The government used the April surplus to repay loans previously taken to finance budget execution. The net repayment totalled UAH 6.6 billion. Also the government pumped additional UAH 3.5 billion of cash into the economy.

Industrial Production by Sectors, % yoy
(To corresponding month of previous year)



Source: State Statistics Committee, the Bleyzer Foundation

Industrial Production by Regions, % yoy
(To corresponding month of previous year)



Source: State Statistics Committee, the Bleyzer Foundation

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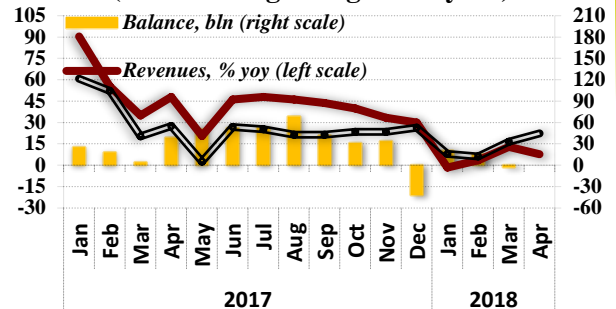
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The growth of consolidated budget revenues turned negative in April. This was due to negative changes in revenues from special-purpose funds (funds confiscated from Yanukovich through court decisions were transferred to the special-purpose funds in April 2017), while both tax and nontax revenues continued to expand (by 28.5% yoy and 56.7% yoy respectively). Tax revenues increased mainly thanks to receipts from the VAT. High growth was observed also in receipts from personal income taxes thanks to growth of nominal wages. At the same time, receipts from the excise tax declined due to drop in production of several excisable goods. Nontax revenues expanded thanks to the second tranche of funds received from sale of the 4G licences and the NBU's transfer of a share of its profits. The cumulative consolidated budget revenues grew by 7.6% yoy in January-April.

Dynamics of consolidated budget components (from the beginning of the year)

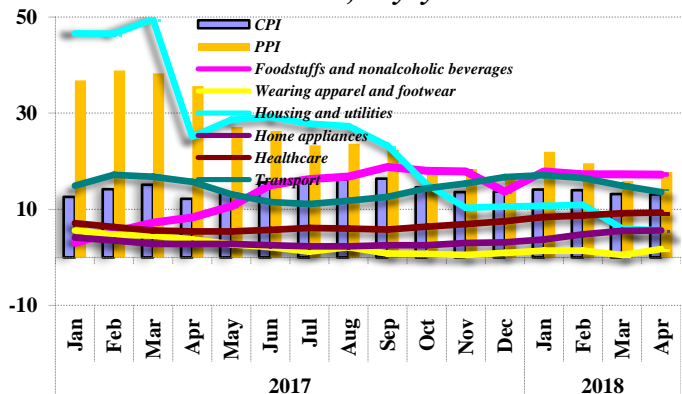


Source: The Ministry of Finance of Ukraine, The Bleyzer Foundation

Consolidated budget expenditures grew at an accelerated rate of 40.5% yoy in April. This expenditure growth was due to increases in all major items of expenditures, except for expenditures on debt servicing. Social security expenditures, current transfers, expenditures on goods and services were the drivers of growth in current expenditures (38.6% yoy). Capital expenditures expanded by 80.2% yoy. Growth of the cumulative consolidated budget expenditures accelerated to 22.2% yoy in January-April.

Payments of the government and the NBU on external debt servicing were lower in April as compared to March. Total principal and servicing payments on external debt denominated in foreign currency amounted to USD 127.4 million. This includes USD 30.8 million of servicing payments on sovereign bonds denominated in foreign currency. The ministry of finance has recently stated that government debt service for 2018 is under control, but IMF financing will be needed in 2019 to serve about \$8.0 billion of debt due to the end of 2019.

CPI, PPI, and Growth of Prices for Select Goods and Services, % yoy



Source: State Statistical Service of Ukraine, The Bleyzer Foundation

Monetary Policy

Inflation. Consumer inflation saw little changes in April. The all items index declined by 0.1 percentage point to 13.1% yoy. Continued supply-driven growth in foodstuff prices remained the major driver of inflation. Increased production cost and fast recovery of consumer demand also made significant contribution to growth of consumer prices. Core inflation remained stable at 9.4% yoy.

Most of the major groups of goods and services saw little or no changes in price growth in April. Wearing apparel and footwear reported the largest acceleration in price growth from 0.5% yoy to 1.7%. On the other hand, communication and transport services saw the largest deceleration in price growth (by 1.5 percentage points to 8.4% yoy and by 1.3 percentage points to 13.6% yoy respectively).

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Banking Sector. In April, growth of the national currency deposits recovered from the deceleration observed a month ago. In fact, the growth of hryvnia deposits accelerated to 14.7% yoy thanks to more than doubled growth in corporate sector deposits which more than offset some deceleration in growth of the household deposits. On the other hand, foreign currency deposits denominated in USD sustained a major growth deceleration to 0.9% decline, leading to a reverse of its growth trend. Foreign currency deposits saw their growth decelerating by 8.5 percentage points to a 0.9% yoy decline, despite almost the same growth in both corporate and household deposits as compared to March.

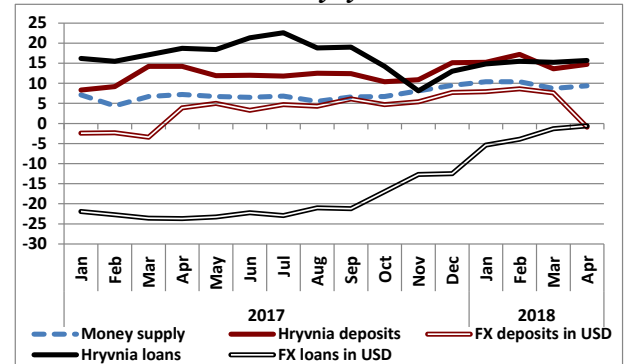
The situation with bank lending activities further improved in April. National currency loans expanded at a rate of 15.7% yoy, while foreign currency loans denominated in USD saw their rate of decline decelerating to 0.6% yoy. Growth of the national currency loans accelerated mainly on the back of faster expansion of household loans. At the same time, deceleration in decline of the foreign currency loans denominated in USD was the result of both slower decline in household loans and faster growth of corporate loans.

Significant increase in cash resources together with expansion of balances at the correspondent accounts of banks caused a 4.8% mom growth of the monetary base, accelerating its over-year growth to 1.9% yoy. Growth of money supply also accelerated (to 1.9% mom and 9.4% yoy) thanks to inflow of deposits in both national and foreign currency during the month. Both, the growth in the monetary base and money supply remained below the rate of inflation.

Hryvnia Exchange Rate. The UAH/USD exchange rate again saw little changes in May. There was some short-term depreciation at the beginning of the month but then the exchange rate turned to gradual appreciation. Overall, the exchange rate appreciated from 26.20 UAH/USD to 26.12 UAH/USD during the month.

The NBU continued liberalizing foreign market regulations in May. First, borrowers of foreign currency can buy foreign currency for purposes of foreign currency loan repayments or servicing at any bank in which he/she has a foreign currency current account, not only at the bank which provided the loan. Second, the regulator allowed nonresidents to purchase and repatriate foreign currency in cases they made investments in the form of dividend reinvestment. Finally, starting on May 16th, banks can make linked settlements on trade operations with foreign currency and bank metals both before and after confirmation of trade agreements with foreign currency and bank metals in the System of Agreements Confirmations in the interbank foreign exchange market of Ukraine.

Dynamics of Money Supply, Deposits, and Loans, % yoy



Source: The NBU, The Bleyzer Foundation

Dynamics of the Average Weighted UAH/USD Exchange Rate in the Interbank Forex Market



Source: The NBU, The Bleyzer Foundation

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International Trade and Capital

In April 2018, Ukraine's current account of the balance of payments achieved a surplus of USD 175 million, compared to a deficit of USD -628 million in March. Such improvement was caused by a surplus in the primary income account of USD 308 million, a surplus of USD 252 million in the secondary income account, and a reduction in the deficit of the merchandise and services trade account to USD -385 million.

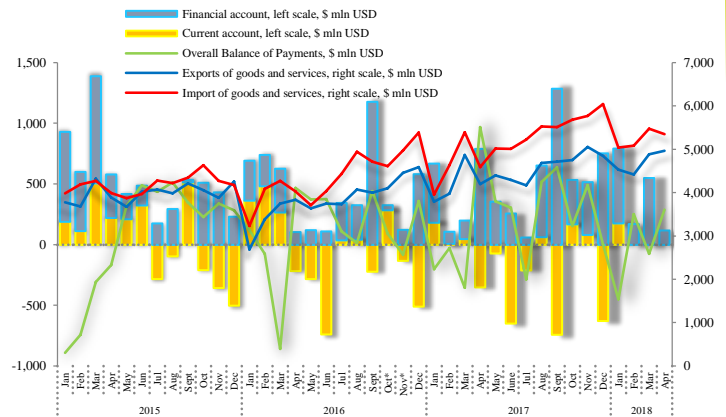
In April 2018, merchandise exports increased by 20% yoy, while imports increased by 18% yoy. The most significant improvements in Ukraine's merchandise exports in April took place in ferrous and nonferrous metals products, which increased by 65.8% yoy in April and reached USD 1,028 million (about 27.9% of total exports). Exports of other sectors also showed a positive growth rate, as follows: wood products (rose by 35.6% yoy), chemicals (24.3% yoy), machinery & equipment (18.8% yoy), industrial goods (16% yoy) and agricultural products (8.1% yoy). On the other hand, negative growth rates took place in minerals and informal products, which declined by -13.1% yoy and 10% yoy, correspondingly. On the import side of the balance of payments, during the month, each sector of goods provided positive growth, as follows: informal trade (34.2% yoy), agriculture (24.6% yoy), machinery and equipment (21.6% yoy), timber and wood (20.7% yoy), metallurgy (15.6% yoy), chemicals (14.8% yoy), industrial goods (14.3% yoy) and mineral products (9.4% yoy).

Regarding the geographical distribution of exports, in January-April 2018 exports to Europe increased 25.9% yoy, whereas exports to the CIS countries increased by 7.5% yoy. The share of Ukrainian merchandise export to Europe reached 38% of total Ukrainian exports, whereas the share of the CIS countries was 16% (7% Russia), compared to 16.5% in January-April 2017. Asia continues to be the largest recipient of Ukrainian exports taking 31% of the total share (growing by 3.8% yoy). The US had a small share of 2% (America 3%) of total Ukrainian exports, but it had the largest growth rate of 24.8% yoy (America, 31.8% yoy).

In January-April 2018, Ukrainian imports from CIS countries increased by 22% yoy (26% of the total), with imports from the Russian Federation increasing by 31% yoy (shares 15% of the total import amount). The share of Europe in imports increased to 39% (with a growth of 7.5% yoy) in January-April 2018. Asia supplied 21% of Ukrainian imports (20.3% yoy growth). Finally, the largest merchandised deficit (export minus imports) in trade turnover took place with CIS countries, with USD -2,036 million (84% of the total) deficit, including Russian Federation with a USD -1,600 million deficit (64% of the total).

In April 2018, Ukraine financial account net inflows amounted USD 119 million, compared to USD 551 million in March 2018. These financial inflows were generated principally by private sector inflows. Foreign direct investments reached USD 98 million, 98% of which directed to the real sector of Ukraine. As a result of surpluses in the current and financial accounts in April, the overall balance of payments had a surplus of USD 290 million, compared to a deficit of USD 75 million in March. This April surplus increased the level of international reserves to USD 18.4 billion as of the end of April 2018 (equivalent to about 4.5 months of imports).

Ukraine's External Balance of Payments, mln USD



Source: NBU, the Bleyzer Foundation

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