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Resume

- According to the IER, GDP in August declined by 2.1% yoy, compared to growth of 4.4% yoy in July, reflecting faster completion of early harvesting in 2024.
- In August, power outages decreased, contributing to enterprises' activities.
- Naftogaz has started importing natural gas from the EU, which will be stored in the "customs warehouse" regime and will be used only in case of emergencies and only for business needs.
- During the year of operation of the Ukrainian Sea Corridor, it transported 64.4 m t of cargo.
- According to the State custom service, exports in August amounted to USD 3.42 bn, while imports amounted to almost USD 5.9 bn.
- In August, state budget revenues were record-high: UAH 448 bn, 2.5 times higher than in August 2023 due to a record amount of grants of UAH 228 bn.
- The Parliament adopted amendments to the State Budget for 2024 to increase funding for defense and security.
- Tax changes that should help finance higher defense spending have not yet been finalized. The main discussions are about the feasibility of 50% of the CIT for banks.
- The Government has submitted a draft State Budget for 2025 to the Parliament. External financing is planned of more than USD 38 bn. However, it is not yet clear who will provide such funding.
- In August, inflation accelerated again to 7.5% yoy compared to 3.3% yoy in May.
- Since the second half of July, the hryvnia has remained in the 41.0-41.5 UAH range per US dollar.

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GDP and Real Sector: Volatility due to changes in harvest time

According to IER, GDP in August declined by 2.1% yoy, compared to a growth of 4.4% yoy in July. This decline reflects the faster completion of early harvesting in 2024, resulting in gross value added (GVA) in agriculture soaring in July, but there has been a sharp decline in GVA in the sector this month.

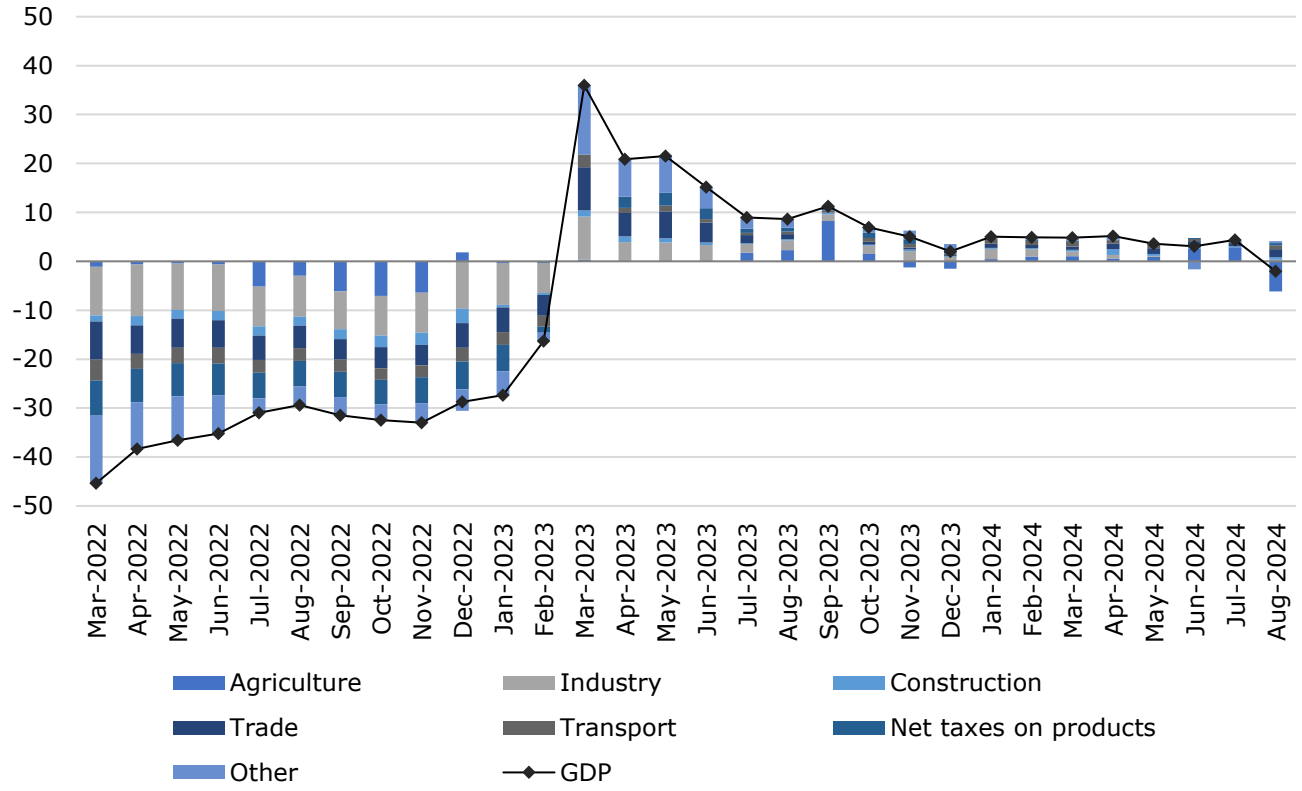
Value added in agriculture fell by 23% yoy because harvesting wheat and other crops was faster than in 2023. Accordingly, most of the early crops were harvested in July, when the estimated real GVA in the sector increased by 27% yoy, leaving less harvest for August this year. Harvesting of corn and sunflower also started earlier, but this could not compensate for the decline of other crops. Yields remained below the record level of 2023. Therefore, this year's harvest is generally estimated to be smaller than last year's. In animal husbandry, the real GVA was estimated to be close to last year's, as reductions in the number of cattle and milk yields were offset by moderate growth in poultry and pig populations.

According to our assessment, the situation in other sectors has not changed significantly. The growth of GVA in the manufacturing industry accelerated to 4.8% yoy in August compared to 3.4% yoy in July. The food industry, mechanical engineering, and metallurgy continued to grow. This growth was facilitated by a better situation with access to electricity, which is also reflected in the respondents' answers in the monthly business survey conducted by the IER. Completing of repairs at nuclear power plants reduced the electricity shortage before new attacks at the end of August. Although electricity supplies were more stable in August, the estimated real GVA in the industry was lower than in August 2023.

Production in the mining industry increased by about 1% yoy. The increase in gas production offset the decline in coal and iron ore production.

The business remains optimistic about the growth of production, sales, and exports in the near term. At the same time, the level of uncertainty remains high.

Figure 1: Contributions to real GDP, p.p.



Source: IER assessment

Soaring wages and the already ongoing full-scale war are contributing to an increase in consumption (partly due to deferred consumption), resulting in retail trade turnover continuing to grow rapidly. At the same time, wholesale trade, although growing, is growing at a very moderate pace.

Therefore, according to our estimates, the growth of real GVA in trade is estimated at 7% yoy, which is close to July.

Several key factors influenced the growth rate of GVA in transport. Ukrzaliznytsia reported an increase in transportation by 15% yoy. This increase was facilitated by the fact that in August 2023, there were virtually no exports from the seaports of Odesa, which now actively continues to work. However, exports from the Danube ports were negatively affected by low waters.

Energy: Ukraine prepares for winter

Electricity. In August, Russian attacks on Ukraine's energy system resumed, so the energy supply situation remains fragile. As a result of the attacks on August 26, units 1, 3, and 4 of the Rivnenska NPP were de-energized and disconnected from the grid, and the capacity of the Pivdennoukrainska NPP was reduced.

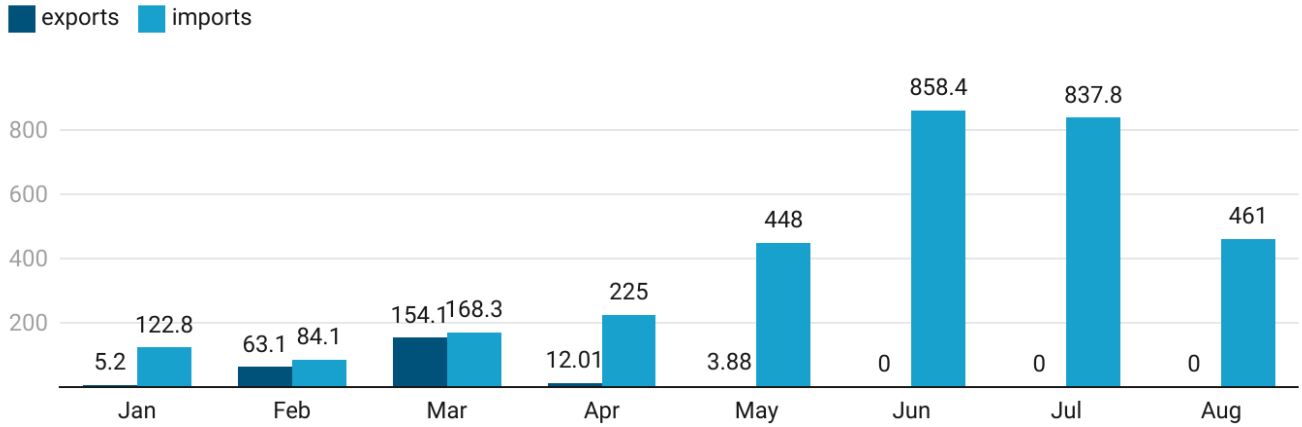
Prime Minister Denys Shmyhal said that the readiness of protective structures at Ukrenergo facilities exceeds 85%. He also noted that it is possible to get through the winter without blackouts, in the absence of new attacks on energy infrastructure, but the absence of attacks is unlikely. In general, the government has allocated UAH 10 bn for the arrangement of passive protection for energy facilities, and more than UAH 5 bn was allocated by Ukrenergo. In January-August, DTEK Energy invested more than UAH 2.1 bn out of the planned UAH 3.9 bn in repairs and restoration of thermal power plants.

In August, Ukraine continued to reduce electricity imports, falling by 45% compared to July to 461 thousand MWh. There were no electricity exports. The largest share in the structure of imports is still taken by Hungary – 44%, in second place – Slovakia (25%), in third place – Romania (17%), the rest – Poland and Moldova. In August, Ukraine attracted emergency aid from Poland and Slovakia for at least seven days.

Analysts note that at the end of August, electricity imports fell due to high prices in European countries caused by the shortage formed against the backdrop of heat and repairs at nuclear power units in the South-Eastern Europe. In addition, the damage to Ukrenergo's substations in many areas as a result of shelling on August 26 made it impossible to deliver electricity to industrial consumers physically, and they were limited even if imported.

From the end of July, when the Laws on the abolition of duties and VAT on the import of certain types of energy equipment came into force, until the beginning of September, Ukrainian consumers delivered to Ukraine batteries, generators and other equipment worth UAH 7 bn, including 120 thousand batteries of various types, and 1800 generators. Through benefits, the Government is encouraging the population and businesses to provide alternative power sources before winter. Customs benefits will be valid until the end of martial law or until January 1, 2026.

Figure 2: Electricity exports and imports in 2024, thousand tons MWh



Source: Energy Map

The National Energy and Utilities Regulatory Commission (NEURC) has simplified the procedure for installing generating units. The time for processing a request for exemption from certain requirements of the Transmission System Code by both system operators and the National Energy and Utilities Regulatory Commission (NEURC) was reduced, the requirements for conducting a cost-

benefit analysis were removed, etc. This solution should simplify and speed up the procedure for installing gas turbine, gas reciprocating, cogeneration and other new and used generating units.

In August, Ukrenergo held the first procurement auctions for five-year contracts to provide ancillary services to balance the power system. On average, 240 MW of reserves were purchased for the system loading service, more than 41% of the auctioned need. Also, an average of about 260 MW of loading and unloading (energy storage) services were purchased every hour - 62% of the need. Ukrenergo also purchased frequency support services from 99 MW energy storage systems.

Gas. Naftogaz has started importing natural gas from the EU, which will be stored in the "customs warehouse" regime and will be used only in case of emergencies and only for business needs. The first deliveries will take place in September 2024. The entire reserve stock will be purchased withthe EBRD loan funds of EUR 200 m.

Oil. The law signed by the President on increasing the excise tax on fuel provides for a gradual increase in the excise tax on gasoline, diesel, and autogas to the minimum level established in the European Union. In particular, from September 1, 2024, to January 1, 2025, the excise tax rate on gasoline should be EUR 242.6 per 1000 liters, diesel EUR 177.6, and gas EUR148. It will increase yearly, and in 2028, it should be EUR 359 per 1000 liters for gasoline, EUR 330 for diesel, and EUR 250 for gas.

Transport: the decline in rail traffic has stopped

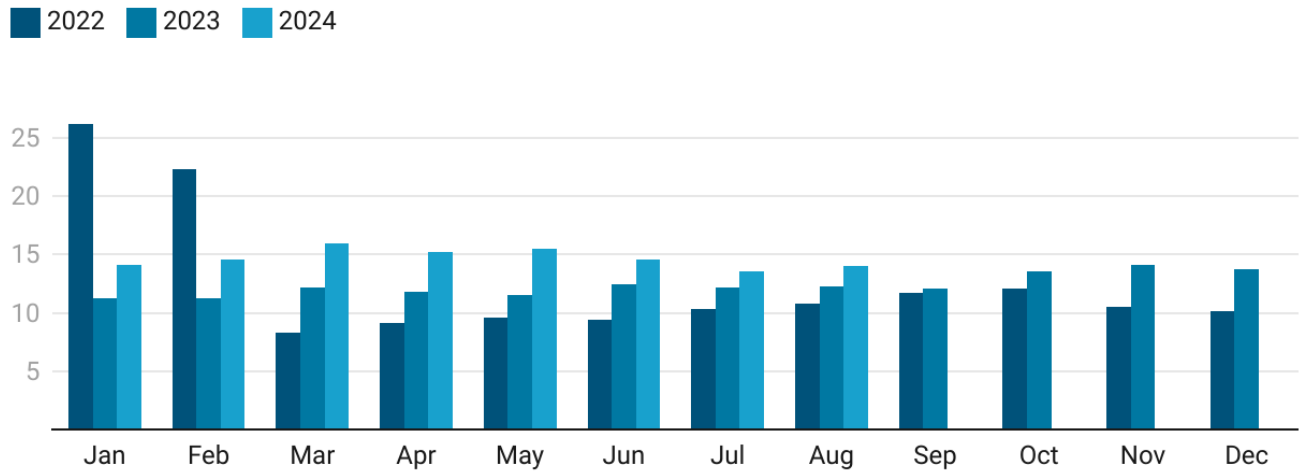
Maritime transport. During the year of operation of the Ukrainian Sea Corridor, it transported 64.4 m t of cargo, of which 43.5 m t were grain. The port of Pivdennyi handled the most cargo - 27.6 mn t, second among the ports of Greater Odesa was Chornomorsk with 21.6 m t, and Odesa the third with 15.2 m t. This port is a leader in the transshipment of agricultural products. In August, seaports handled 6.8 m t of cargo, 8% more than in July. Of these, 4 m t were agricultural products.

Container shipping is being resumed. Thus, since the beginning of April, the Chornomorsk Port has received 46 container ships and processed 35 thousand TEU.

At the same time, the load on the Danube river ports is falling, and the Ukrainian Danube Shipping Company is switching to a 6-hour working day to reduce costs. The company also suspended all investment projects except for modernization. Work on the Danube is also complicated by the abnormal heat, which causes the Middle Danube to become shallow.

Rail transport. Ukrzaliznytsia transported 14.2 m t of cargo in August, 4% more than in July and 14% more than in August 2023. Export shipments to the western border in August amounted to 2.8 m t, a decrease of 2% mom. Transportation toward seaports amounted to 4 m t (an increase of 6.5% mom). Grain and flour were the major commodities transported to ports and the border (2.6 m t), followed by ores (2.32 m t) and ferrous metals (0.57 m t).

Figure 3: Transportation of goods by rail, million tons



Source: Ukrzaliznytsia

Foreign trade: Exports returned to USD 3.4 bn

Exports in August, according to customs, amounted to USD 3.42 bn. Thus, it returned to about USD 3.4 bn, which was observed in January-May this year. A more reliable electricity supply in August may have played a role. However, the State Customs Service also raised its estimate of exports in January-July this year from USD 22.7 bn to USD 24.2 bn. It is not yet known whether this revision will be reflected in official trade statistics, but it may reflect changes in the reporting methodology of the State Customs Service. Exports of agricultural products reached USD 1.91 bn in August, the highest figure in the three summer months but lower than USD 2.16 bn on average in January-May. Exports of wheat and rapeseed, harvested in early August, increased, while exports of corn and sunflower oil (harvesting of corn and sunflower began at the end of August) fell further as stocks declined last year.

Figure 4: Trade in goods of Ukraine, 2021-2024, USD bn



Source: State Customs Service of Ukraine

Exports of metallurgy products amounted to USD 438 m in August, the best result this year. Exports of pipes and rolled products increased partly due to decreased exports of semi-finished steel products. After the revision of export figures, exports of other types of products increased the most, primarily industrial products and engineering products (including cables, furniture, and heating devices). These goods are often produced using tolled (ie not owned by the producer) raw materials. In August, exports remained close to the revised January-July figures.

Imports in August decreased slightly to USD 5.89 bn compared to USD 5.93 bn in July but remained high. In particular, imports of machinery and equipment remained high. Thanks to new VAT and import duty exemptions and high needs, imports of generators and batteries continued to grow despite better electricity supplies in August. Due to the increase in excise duty from September 1, gasoline imports also increased in August: companies tried to bring as much fuel as possible at the old rates. At the same time, imports of chemical products, including medicines and food products, slightly decreased.

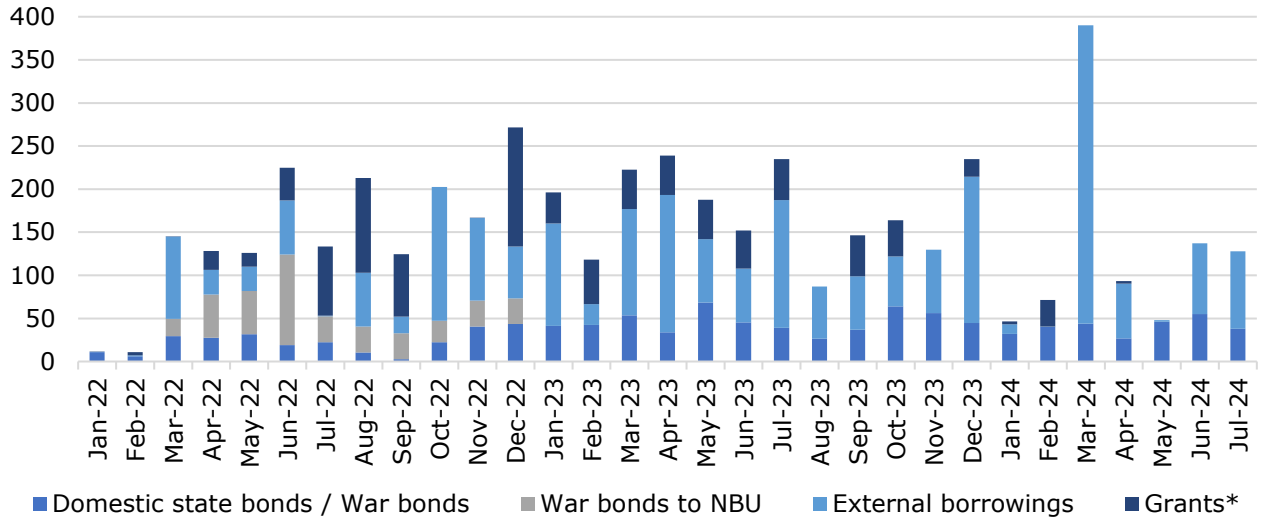
Fiscal policy: Tax changes have not yet been adopted

Budget execution: In August, state budget revenues were record-high: UAH 448 bn, 2.5 times higher than in August 2023 due to a record amount of grants of UAH 228 bn. Thus, USD 3.9 bn was received from the United States. This amount is half of the budget support approved in May (the other half is likely to arrive by the end of 2024). The EU also provided a grant of EUR 1.5 bn as part of budget support under the Ukraine Facility. Within this framework, The mechanism received EUR 2.7 bn in concessional loans (the European Union covers the interest rateby) due to Ukraine's implementation of all the steps envisaged in the Plan of Ukraine for the second quarter of this year approved by the Government.

In August, revenues without grants increased by 23.9% yoy. In particular, corporate income tax revenues increased by 36.6% yoy due to higher tax payments by banks (due to higher revenues

and higher tax rate of 25% instead of 18% of the general rate). Consumption growth explains higher VAT revenues (both domestic and imported) by 17% yoy. At the same time, VAT refunds of UAH 12.2 bn were 36% higher than last year.

Figure 5: Funding and grants received by the state budget, UAH bn



Note: * Grants are part of budget revenues, which are accounted for under the code 42000000 "Official transfers from the EU, foreign governments, international organizations, donor institutions".
Source: Ministry of Finance

Overall, revenues administered by the State Tax Service (STS) exceeded the plan by 5.2%. In comparison, the State Customs Service (SCS) collected 92.2% of the tax revenue plan in its area of responsibility. At the same time, in the first eight months of this year, the State Tax Service and the State Migration Service exceeded the revenue plan by 10% (or UAH 63.3 bn) and 3.3% (by UAH 12 bn, respectively).

In August, state budget expenditures were also a record UAH 361 bn, and the budget balance was in surplus. Nevertheless, expenditures during the eight months of 2024 were significantly underperformed. This situation resulted from both planning problems and the need to save money on financing non-priority expenditures. Funding for reconstruction and recovery remained below 2023 levels.

In August, borrowings in the domestic market were low (only UAH 27.7 bn), and the Ministry of Finance tried not to raise interest rates. In general, in August, the attracted financing from the placement of domestic government bonds was less than the repayment and interest paid on domestic debt. At the same time, borrowings in the domestic market increased at the beginning of September. During the two auctions in September, the placement of domestic government bonds amounted to UAH 40.8 bn, in particular, due to the issuance of foreign currency securities. Another reason for the success was that the banks received significant funds from the repayment of previously issued government bonds. However, the third auction in September was not so successful and brought the Government only UAH 13.8 bn, which is higher than the average of all previous months but less than the need to fulfill the probable plan by the end of the year after the expected revision.

Changes: After numerous discussions, the Parliament prepared and adopted its own version of the draft law on changes to the state budget for 2024. As previously planned, expenditures should increase by almost UAH 500 bn, of which slightly more than UAH 370 bn for programs of the Ministry of Defense and about UAH 110 bn for the structures of the Ministry of Internal Affairs. At the same time, the vision of financing such an increase in expenditures has changed. Part of this is cutting other costs. In particular, UAH 115 bn are the savings on repayment and servicing of external debt due to the successful restructuring of public debt.

Planned revenues increased due to the already overfulfilled revenues, as well as UAH 30 bn from planned tax changes and the decision to increase the excise tax rate on fuel from September 2024. However, a significant source of funding for larger expenditures should be the placement of domestic government bonds: net borrowings for UAH 216 bn. This is a very ambitious amount,

which indicates that the weekly placement of domestic government bonds should bring about UAH 20 bn by the end of the year.

On September 17, MPs finally voted for the basis of amendments to the Tax Code, designed to help increase tax revenues. Although it was previously assumed that the relevant changes should bring an additional UAH 140 bn to the budget in 2024 and UAH 340 bn in 2025, the voted changes can help to get only UAH 58 bn in 2024 this year and UAH 137 bn next year. Of the envisaged changes, there is an increase in the military tax to 5% for employees, the introduction of a military tax for sole proprietors under the simplified taxation system, and 25% of the CIT for financial institutions. After heated discussions, the deputies voted on 50% of the CPT rate for commercial banks. At the same time, the government and MPs have abandoned the idea of raising the VAT rate by several percentage points, which was proposed by several experts, including the IER. Therefore, financing expenditures until the end of 2024 remains risky, and we are talking about defense and security expenditures.

State Budget-2025: On September 13, the Government approved the draft State Budget 2025. The budget indicators are based on the macroeconomic forecast approved by the Government, which assumes that in 2025, real GDP will grow by 2.7%, and nominal GDP will amount to UAH 8466 bn, which is quite close to the IER forecast. At the same time, inflation is forecast to accelerate to 9.5% yoy in December 2025, and the exchange rate will devalue from 40.8 UAH/USD up to 45,0 UAH/USD: in the IER forecast, inflation and devaluation are expected to be somewhat slower.

State budget revenues are envisaged for UAH 2336 bn, which is 22% higher than the revised figure for 2024. They will grow from 25.5% of GDP to 27.6% of GDP due to planned tax changes and an increase in the planned transfer of NBU revenues to the state budget to UAH 63.9 bn (UAH 38.6 bn in fact in 2024).

Table: Key Macroeconomic Indicators

Name	2023	2024		2025
	Report	Decree CMU from 15.12.2023 № 1315	Expected by MinEconomy (as of 28.06.2024)	Decree CMU from 28.06.2024 № 780
GDP:				
nominal, UAH bn	6 537.8	7 643.0	7 484.7	8 466.3
real change, % yoy	5.3	4.6	3.5	2.7
CPI, % December, yoy	5.1	8.5	5.4	9.7
Trade balance, USD bn	-37.7	-40.2	-41.0	-40.7
Exports of goods and services, USD bn	51.1	56.3	53.5	57.2
Imports of goods and services, USD bn	88.8	96.4	94.4	97.9

Source: Explanatory note to the draft State Budget for 2025

State budget expenditures are planned for UAH 3999 bn, which is only 6.8% higher than the revised figure for 2024. At the same time, expenditures on the programs of the Ministry of Defense will increase by only 2% compared to the figure voted on September 17.

Funding for the Ministry of Social Policy programs will decrease by 8.9%, primarily due to the lower planned transfer to the Pension Fund. To this end, the Government envisages the resumption of the mandatory payment of SSC by all sole proprietors, as well as the transfer of funds in the accounts of Oschadbank for the payment of pensions that have not been made.

Expenditures on financing the programs of the Ministry for Communities and Territories Development (both direct and national) are growing rapidly. In particular, the financing of the Road Fund (to which part of the revenues from excise taxes on fuel is directed) is partially restored. Funding is also provided for programs for the restoration, development of municipal transport, and reconstruction of housing and infrastructure.

The state budget deficit is envisaged of UAH 1640 bn or 19.3% of GDP. It will be financed primarily by external borrowing. Although external loans are expected to amount to USD 38.8 bn, to date, there has been no confirmation of at least half of this amount. Probably, the Government expects to receive a large part of the funds from the package of USD 50 bn approved by the Group of Seven from Russian assets, but this solution is now stuck. Instead, the EU is considering the possibility of providing Ukraine with a similar package of EUR 20-40 bn without the participation of the United States. The planned placement of domestic government bonds exceeds the repayment by only UAH 17 bn, less than the interest on already issued securities.

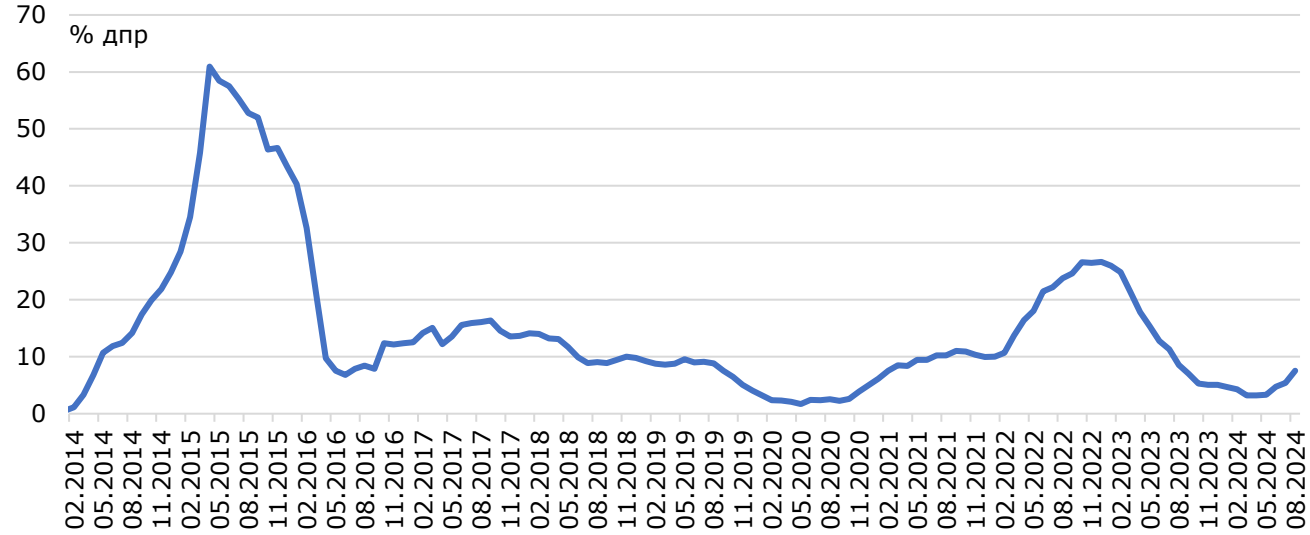
The budget parameters may still change before the second reading, as the forecast may be updated, and the final version of the tax amendments has not yet been adopted. To date, the Government and the IMF have already reached an agreement at the expert level on the fifth review of the Program, but the decision of the IMF Executive Board is expected in mid-October. The IMF's decision may depend on the actions of the Government and the Verkhovna Rada regarding the budget.

Inflation: Consumer inflation accelerated again in August

Inflation accelerated again to 7.5% yoy in August compared to 3.3% yoy in May. Rising producer and retailer costs for imports, electricity and labor (average wages increased by more than 22% yoy in Q2 2024) and the gradual recovery of consumer demand after the sharp drop in 2022 probably played a role here. However, unfavorable weather conditions also added to the CPI increase: due to the lack of rain, prices for several vegetables increased sharply compared to the previous year: according to the State Statistics Service, the average price of cabbage has almost tripled, and potato prices increase by more than 50% yoy.

In monthly terms, prices increased by 0.6% mom in August, although they usually decline in August due to a seasonal drop in prices for vegetables, fruits, and clothing. However, due to the poor harvest of some vegetables, in particular, a sharp rise in the price of cabbage, vegetables on average rose in price by 5% mom instead of the typical 10-20% mom price decrease. While the seasonal decline in fruit and clothing prices did occur, prices for a wide range of goods and services increased due to rising costs. Excluding changes in prices for vegetables, fruits and clothing, prices increased by an average of 0.8% mom.

Figure 6: Consumer price inflation



Source: State Statistics Service of Ukraine

Exchange Rate and Monetary Policy: NBU Council Reaffirms the NBU's Current Monetary Policy Direction

Monetary policy. The Council of the National Bank of Ukraine (NBU) approved the new Monetary Policy Guidelines, which determine the direction of the NBU's monetary policy. The Council confirmed the decision of the NBU leadership to move away from a fixed exchange rate and switch to "flexible" inflation targeting, which takes into account the state of the economy under the martial law. The inflation target was confirmed at 5%, but considering possible greater deviations from the

target due to the war and the need to limit fluctuations in the hryvnia exchange rate. They also recognized the need to maintain interest rates in hryvnia at a relatively high level to limit the demand for foreign currency.

Exchange rate. Since the second half of July, the hryvnia has remained in the range of 41.0-41.5 UAH per US dollar. However, the NBU continues to spend a significant share of the Government's foreign currency inflows to balance supply and demand for foreign currency. The NBU's interventions amounted to USD 2.8 bn in the four weeks ended September 16. This decision aligns with the average level of NBU interventions in the summer, but higher than in previous months. There was a significant deficit in foreign trade, and the net demand for cash foreign currency, although slightly decreasing, remained relatively high.

NBU's international reserves rose to USD 42.3 bn at the end of August. They returned to the May level after receiving the next tranche from the EU for the Ukraine Facility and funds from the United States through the World Bank totaling USD 8.5 bn. At the same time, USD 1.1 bn was spent to service the external debt and USD 2.7 bn NBU interventions to balance the FX market. According to the NBU, the reserves can finance 5.4 months of imports.

Figure 7: Official exchange rate of the hryvnia to the US dollar (UAH per USD)



Note: Note that the exchange rate values in the figure start at UAH 36 per USD. United States.
Source: NBU

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