Monthly Economic Monitor Ukraine

No.11 (181), November 2015

EXECUTIVE SUMMARY

HIGHLIGHT: TRADE WITH RUSSIA

Politics: Regular local elections were held on October 25. No party was able to gain a majority in any oblast (regional) council.

Real sector: Decline in industrial output decelerated further to 5.1% yoy which partly reflects stabilisation of the situation in the East of Ukraine.

Energy sector: In October, Ukraine imported 2.4 bn cubic meters of gas (bcm): 2 bcm from Russia and 0.4 bcm from Europe.

Agriculture: Gross agricultural production in September decreased by 4.2% yoy due to lower crop harvest and decline in livestock production.

External sector: Current account balance in September was positive at USD 0.1 bn as slight deficit of trade in goods was compensated by positive net exports of services.

Fiscal policy: Higher than planned revenues, lower than planned debt and subsidy costs, delays in appropriating extra revenues resulted in the surplus of central government and local governments.

Social policy: Between January and September the number of families that were granted housing and utility subsidies increased by 5.4 times to 2.6 million.

Labour market: Real wage declined by 18.6% yoy as a result of bad financial results of companies, high inflation, and weak labour market.

Monetary policy: CPI in October fell by 1.3% mom.

Exchange rate: In October, interbank exchange rate remained in UAH 21-23 range set by the NBU but it moved closer to upper end of the range by the end of the month.

State debt: Key international sovereign rating agencies upgraded Ukraine's ratings for obligations in foreign currency.

Highlight of the month: Trade with Russia

THE IMPACT OF RUSSIAN PROTECTIONISM ON THE UKRAINIAN ECONOMY[1]

Mykola Ryzhenkov, Veronika Movchan, IER

It is settled that provisional application of Deep and Comprehensive Free Trade Area (DCFTA) between Ukraine and the EU will start since January 1, 2016. In a response, Russia is expected to increase trade barriers vis-à-vis Ukrainian goods. The decision to launch additional protectionist measures was announced by Dmitry Medvedev, the Prime-Minister of the Russian Federation.[2]

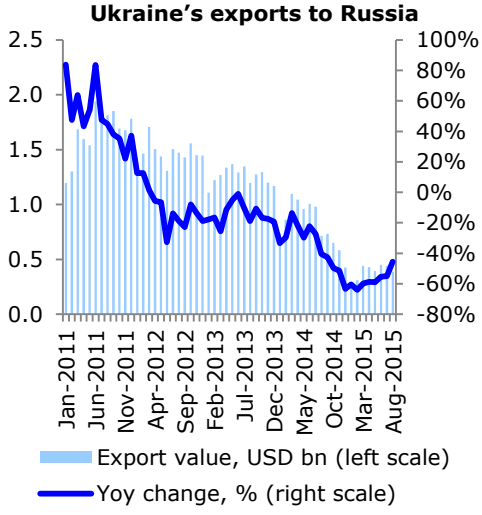
In 2014-2015 the Russian Government passed several decrees that envisage establishment of MFN tariffs and quantitative restrictions in trade with Ukraine as soon as Ukraine will start implementation of the DCFTA. We are referring to two decrees:

- Decree #959 dated 19.09.2014 envisaging unilateral introduction of the MFN duties on about a quarter of Ukraine's trade nomenclature currently exported to Russia;
- Decree #842 dated 13.08.2015 adding Ukraine to the list of countries, against which Russia applies trade sanctions and, thus, imposes embargo on Ukrainian agri-food products.

The question is about severity of the impact of these measures on the Ukrainian economy. Our analysis shows that the impact could be surprisingly low.

To start with, increased protectionism is not a new direction of Russian trade policy regarding Ukraine. Russia has already implemented a number of measures limiting imports. In particular, Ukraine has filed multiple specific trade concerns in the WTO regarding growing number of Russian import bans referred to TBT and SPS issues. As of now, import bans include railcars, confectionery, dairy products, alcohol products, vegetables, soya beans, sunflower seeds, poultry etc. Also, Ukrainian companies have got problems with access to public procurements and with customs procedures. So, producers are aware about potential threats and should have already adjusted their production and external sales plans accordingly.

Ukraine's exports to Russia



Source: Ukrstat

Exports to Russia have already sharply contracted. During second half of 2014 – first half of 2015 Ukraine's exports to Russia amounted USD 6.4 bn, which is only 36% of 2012 value. As a result, the Russian market became less important for Ukraine: in 2012 Russia accounted for 25.6% of Ukraine's exports of goods, whereas in second half of 2014 – first half of 2015 the share decreased to 14.6%. Thus, further contraction of trade with Russia will be less visible in overall exports than it could be few years ago.

Partial equilibrium analysis of trade policy shocks sheds light on the effect of potential policy measures by Russia. The analysis was focused on tariffs and quantitative restrictions, while non-tariff barriers were not taken into account. We used trade statistics for second half of 2014 – first half of 2015 and compared different scenarios of increase in trade barriers by Russia.

The analysis showed that the implementation of Decree #959 and Decree #842 will have rather moderate impact on exports to Russia if compared to current trade drop. To be more specific, application of Decree #959, which impose MFN duties for a number of Ukrainian goods, could potentially decrease exports to Russia by USD 0.23 bn or 3.6% (0.23% GDP). *Ceteris paribus*, pure effect of import ban on agri-food products could lower Ukraine's exports to Russia by USD 0.41 bn or 6.4% (0.41% GDP). Finally, joint application of both measures could lead to contraction of Ukraine's exports to Russia by USD 0.55 bn or 8.6% (0.55% GDP). For comparison, in second half of 2014 – first half of 2015 the export to Russia dropped by USD 6.8 bn or 6.6% GDP.

Table 1. Evaluation of possible scenarios for Russian trade policy vis-à-vis Ukraine

Scenario	***Export reduction***	***GDP equivalent***
Partial FTA cancellation (Decree #959)	USD 0.23 bn	0.23%
Ban on agro-food products (Decree #842)	USD 0.41 bn	0.41%
Partial FTA cancelation (Decree #959) + ban on agri-food products (Decree #842)	USD 0.55 bn	0.55%
Unilateral FTA cancelation	USD 0.90 bn	0.90%

Source: Giucci R., Ryzhenkov M., Movchan V., (2015) Cancelation of FTA between Ukraine and Russia? Estimation of impact on Ukrainian exports. German Advisory Group in cooperation with the IER Kyiv, Policy Briefing Series. PB/11/2015

Moreover, even unilateral cancellation of entire FTA by Russia would have rather moderate direct impact. Ukraine could lose about USD 0.90 bn of exports or 0.90% GDP. The severity of impact of Russian trade measures has vanished with reduction in export dependency on Russian market. Same calculations based on data from 2012, when Ukraine exported USD 17.6 bn to Russia, showed potential impact of unilateral FTA cancellation equal to USD 3.0 bn.

What is a potential for reallocation of lost sales from Russian to other markets? We looked at exports of top-20 product categories (at 4-digit HS), which Ukraine sold to Russia in the first half of 2014, and compared with

trade statistics for the same period of 2015. Results show that for many product categories trade tensions resulted in loss of the Russian market, but no significant alternatives were found. The best prospects for reallocation from Russian market were demonstrated by metallurgy, with many sales reallocated to the US, the EU and Asia. Partial reallocation was observed for machines, food and paper products. Exports of rail cars and chemicals, almost fully dependent on Russian market, did not demonstrate any significant reallocation to other external markets.

To conclude, trade barriers that Russia is expected to introduce in response to the DCFTA application will have moderate impact on Ukraine's exports. Moreover, these measures will be a continuation of current Russia's trade policy regarding Ukraine, and, thus, they have been long anticipated by businesses that should have taken into account this risk into their trade strategies. Still, some time will be required to reallocate sales from the Russian market to the rest of the world.

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[1] The article is based on Giucci R., Ryzhenkov M., Movchan V., (2015) *Cancelation of FTA between Ukraine and Russia? Estimation of impact on Ukrainian exports.* GAG/IER, Policy Briefing Series. PB/11/2015, http://www.beratergruppe-ukraine.de/wordpress/wp-content/uploads/2014/06/PB_11_2015_en.pdf

[2] http://www.epravda.com.ua/news/2015/10/30/565338/

Monthly Economic Monitor Ukraine

Politics: Local election demonstrated increased political fragmentation

Local authorities. On October 25, Ukraine held a regular local election, which took place in all regions except for Russia annexed Crimea, and the occupied areas of Donetsk and Luhansk regions. The election showed a small decrease in the popularity of Solidarnist, President Petro Poroshenko's party (in the election to oblast councils it got 19.4% of votes, a decrease from 21.8% in the parliamentary election of 2014). The election to oblast councils also revealed an increase in support for Yulia Tymoshenko's Batkivshchyna party comparing with the parliamentary election (the party's share of votes increased from 5.7% to 12.0%), the pro-Russian Opposition Block (an increase from 9.4% to 11.5%), and the right-wing Svoboda party (an increase from 4.7% to 6.7%). In addition, a number of new players emerged on the political scene (Ukrop, Vidrodjennia, Za konkretni spravy). The Narodny Front party, headed by Prime Minister Arseniy Yatseniuk, did not take part independently in the election but supported Solidarnist.

No party was able to gain a majority in any oblast (regional) council. In most regions, the largest party would have from 18% to 33% of seats in the council. The only exceptions are the city of Kyiv (where Solidarnist gained 43% of seats in the city council), the oblast of Kharkiv (where the Vidrodjennia party got 42% of seats in the oblast council), and the oblast of Dnipropetrovsk (where the Opposition block got 38% of seats in the oblast council). The mayors of most of the largest cities will be elected in the second of the election on November 15. The voter turnout was 46.6%, which was lower than in the previous local election of 2010 (52.2%) and the Parliamentary election of 2014 (51.8%). Current local election used mainly a kind of a proportional representation voting system (except for election of village councils, which were elected using a single-winner voting system).

Law enforcement. On November 7, the police force officially called 'militia' was replaced with the National Police of Ukraine. However, militia officers would continue to perform their duties until the police staff is recruited. The militia officers may be hired by the police after conformation of their skills and certain checks. The reform is expected to be completed no later than in the end of 2016.

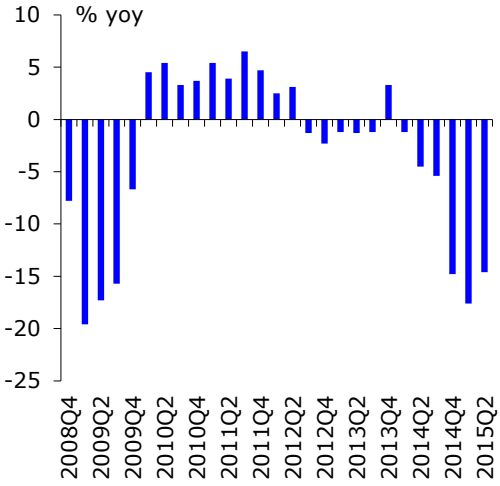
On October 26, the European Commission for Democracy through Law (the Venice Commission) approved the project of the judicial reform drafted by the President's Constitutional Commission. That project aimed at establishing mechanisms for gradual change of judges. But the decision of the Venice Commission might be also interpreted in such a way that it approved also an alternative project of the reform, which was developed by civic activists and made provision for establishment of a completely new system of justice.

Transparency. On October 21, the Government approved a list of about 300 state databases and other data sources that would be made open to the public. The list included the register of legal entities and individual entrepreneurs (FOP), the register of patents, the register of medicines, and financial plans of state-owned enterprises. The data will be available through the web-site data.gov.ua. On October 6, the Ministry of Justice also opened public access to the register of real estate, which contained information on real estate owners. However, in fact the Ministry opened only access to a part of records because the other data did not exist in electronic form.

The EU. In early November, Ukraine made some progress in meeting the EU requirements, the fulfilment of which was necessary for obtaining a visa-free regime for short trips of Ukrainians to the EU. On November 5 and 9, the Parliament passed five laws, adoption of which was a precondition for granting the visa-free regime. The laws regulated confiscation of graft-related assets, provided for establishment of an agency dedicated to recovering such assets, and

Population (without Crimea): 42.7 m
Industry/GDP: 19%
Agriculture/GDP: 10%
Investment/GDP: 14%
Exports to: Russia 18%, EU 32%
Imports from: Russia 23%, EU 39%

Real GDP growth



Source: Ukrstat

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regulated labour migration issues. However, the Parliament did not adopt all necessary laws. In particular, it did not pass an amendment to the Labour Code prohibiting discrimination, including discrimination on the basis of sexual orientation. Ukrainian authorities expected to get the visa-free regime in 2015, but now it is not likely to happen before 2016.

The war in Donbas. In October, Ukraine completed necessary steps to withdraw certain weapons with calibre less than 100 mm from the front line in accordance to an agreement signed in late September. Russia-controlled insurgents declared that they were also withdrawing such weapons. But in the second half of October, the insurgents increased firing against Ukrainian troops, which suggested that an escalation of the conflict was possible.

Real sector: Stabilization continues

Sectoral trends. Decline in industrial output decelerated further to 5.1% yoy. This partly reflects stabilisation of the situation in the East. In particular, industrial production in Donetsk oblast grew by 17% yoy and Luhansk oblast by 13.0% yoy. Metallurgy complex adjusted to some degree to new logistics. Coal extraction increased by 14.9% yoy and iron ore extraction grew by 4.7% yoy. This helped metallurgy increase production by 3.0% yoy. At the same time, decline in machine building accelerated to 9.6% yoy (as compared to 6.3% yoy in August) due to drop in manufacturing of computers and electronic equipment by 38.1%. Production of vehicles grew by 1.3% yoy likely due to defence orders for parts and equipment (production increased by 52% yoy). Food production dropped by 16.9% yoy due to lower purchasing power of households as well as due to delays in harvesting sugar beets. Decline in overall manufacturing production remained at 8.3% yoy.

In September decline in retail sales by enterprises decelerated to 16.3% yoy due to some recovery in purchasing power of households. This reflects decline in disposable households income.

Drop in in construction accelerated to 16.4% yoy due to decline in residential construction by 17.6% yoy. At the same time, investments into infrastructural construction increased probably due to renovation works in the East of Ukraine.

The Ukrstat publishes data excluding temporarily occupied territory of the Autonomous Republic of Crimea and Sevastopol and the territory under anti-terroristic operation in the East. The statistical base was also revised to make like-to-like comparison available.

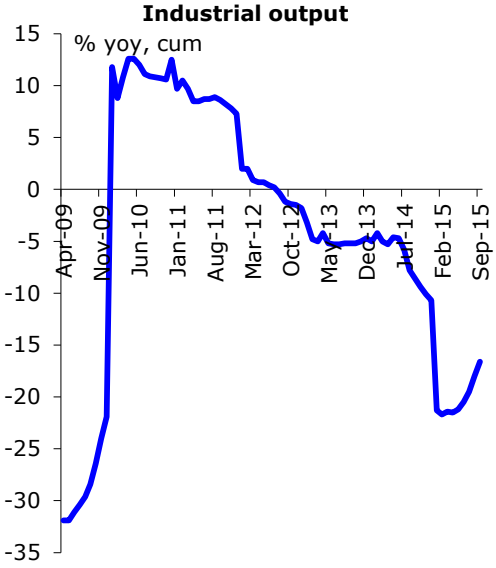
Energy. Competition on the gas market

Gas. On October 12, Ukraine resumed imports of the Russian gas. In October, Ukraine imported 2.4 bn cubic meters of gas (bcm): 2 bcm from Russia and 0.4 bcm from Europe mainly via Slovakia. Overall, between January and October, Ukraine imported 14.8 bcm of gas: 5.7 bcm from Russia and 9 bcm from Europe.

Starting November 1, the Naftogaz of Ukraine introduced differentiated pricing for gas depending on the industrial consumer category and supply conditions. The lowest price of UAH 5739 per thousand cubic meters is set for industrial consumers with gas consumption above 10 m cubic meters of gas per month who are required to pay in advance 110% of the monthly consumption volume. The highest price of UAH 6470 is set for industrial consumers paying after the delivery or according to the contract. The Naftogaz received the right to set gas prices for industrial consumers and budget entities in October with coming into force the law On the Natural Gas Market. The new pricing strategy created competition on the gas market as some of defined by the Naftogaz prices are lower than the prices of private gas companies (around UAH 6100-6300 per thousand cubic meters). For comparison, the average price of imported gas in the second quarter of 2015 was USD 268 or UAH 5810 per thousand cubic meters.

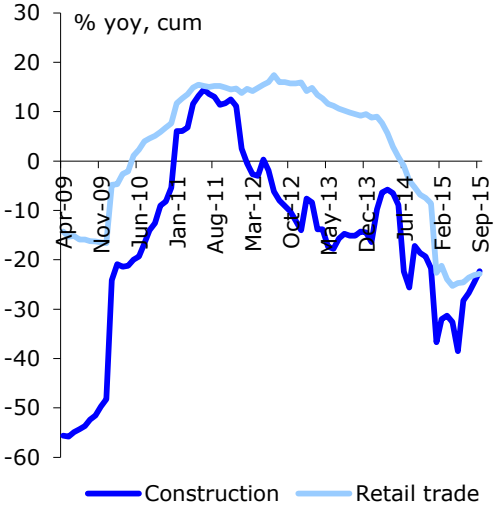
The Cabinet of Ministers postponed from September 30, 2015 till January 1, 2016 the requirements for gas traders to create insurance

Industrial output



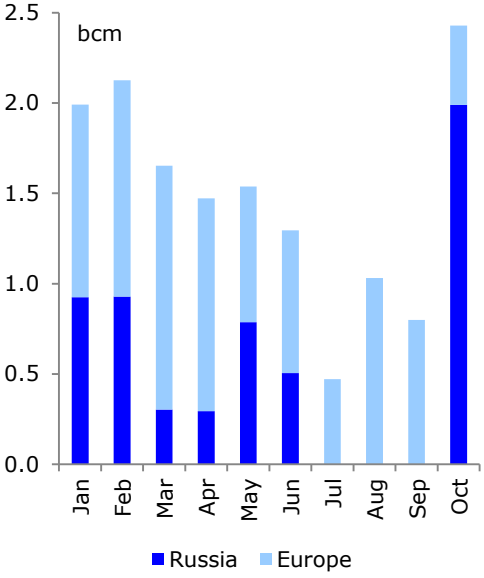
Note: Since April 2014 - data excludes Crimea
Source: Ukrstat

Real sector trends



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

Gas imports in 2015



Source: Ukrtransgaz

gas stocks equal to the monthly supply volume. According to the Energy minister, this grace period is needed for monitoring and analysis of the situation on the gas market.

Agriculture: Negative effects of drought

Production. Gross agricultural production in September decreased by 4.2% yoy due to lower crop harvest and decline in livestock production. As of October 2015, grain harvest was by 1.2% lower than in 2014. Decrease in seeded area due to financial problems and reduction of yields (due to drought in the summer-autumn 2015) resulted in lower harvest of barley (by 9.0% yoy), rye (by 8.8% yoy), oat (by 20.2% yoy), and buckwheat (by 22.6% yoy). All these crops (especially buckwheat) are consumed predominantly on domestic market. Their deficit is likely to result in higher domestic prices and larger imports. On the other hand, wheat harvest increased by 9.3% yoy due to a larger harvested area. Collected volume of sunflower and soybean also increased by 3.6% yoy and 11.2% yoy, respectively.

The drought in the second half of 2015 negatively affected the winter seeding campaign as well. According to the estimates of Ukrainian Hydrometeorological Center, 30.0% of seeded area will not bring harvest. Only 60.0% of area planned for seeding by rapeseed was seeded as of October 2015. There is still time to improve the situation by seeding winter barley in the Southern regions.

Decline in livestock production accelerated to 4.1% yoy due to lower domestic demand and the collapse of trade with Russia.

Agricultural policy. The Agricultural Committee of the Parliament suggested for approval the draft Law on Amendments to section X "Transitional Provisions" of the Land Code of Ukraine on the extension of agricultural land moratorium. The Law was initiated by the group of twenty three deputies and in envisages prolongation of moratorium by one more year. There are large chances that the Parliament will approve this law in the nearest month. This would result in the diversion of potential FDI inflow to agriculture. Also, farmers will be still unable to use their land as collateral, thus they will continue to have restricted access to financing.

External sector: Twin surplus improves

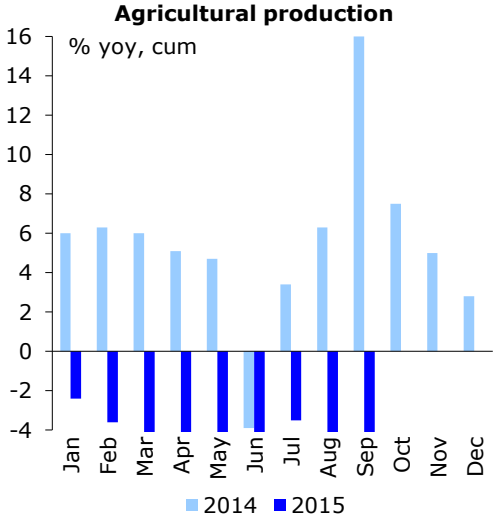
Note: In the analysis we use BPM6 methodology. In particular, since the third quarter of 2014 the NBU started to report balance of payment data based on the Sixth Edition of the IMF's Balance of Payments and International Investment Position Manual.

Current account. Current account balance in September was positive at USD 0.1 bn as slight deficit of trade in goods (at USD 0.1 bn) was compensated by positive net exports of services (at USD 0.2 bn). Merchandise trade deficit decreased as reduction of exports slowed down, whereas drop of imports accelerated.

The factors of exports decline remained unchanged: drop in global prices for essential exports products, disruption in production due to military conflict in the East, and trade tensions with Russia. However, decline in real exports of minerals decelerated, while real exports of metals increased in September (on year-on-year basis). As a result, reduction of overall merchandise exports slowed down to 24.0% yoy (from 28% yoy in August). In particular, exports of metals declined by 23.0% yoy (statistical base effect also contributed a lot), and exports of mineral dropped by 35.8% yoy. Exports of machinery continued to suffer from restricted access to the Russian market, its contraction accelerated to 39.1% yoy. Restricted access to natural gas continued to influence exports of chemicals, which drop accelerated to 42.7% yoy because of statistical base effect. Decline in exports of agri-food products at 14.1% yoy is explained by decline in world prices, which more than counterweighted higher physical volume of exports. Exports of services contracted by 12.6% yoy.

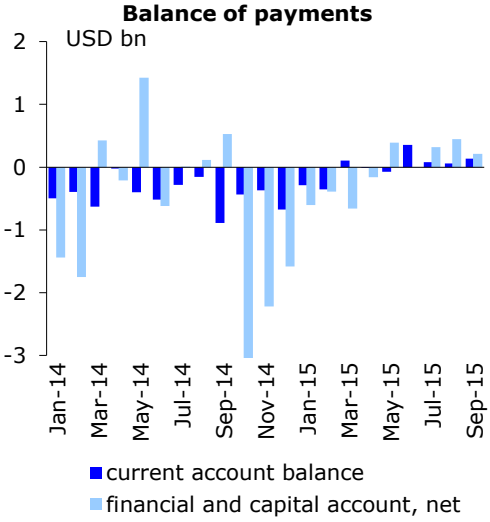
Decline in imports accelerated to 27.2% yoy due to high statistical base (comparing to August 2015, imports in September increased by 3.0% mom). Food imports contracted by 39.2% yoy due to lower

Agricultural production



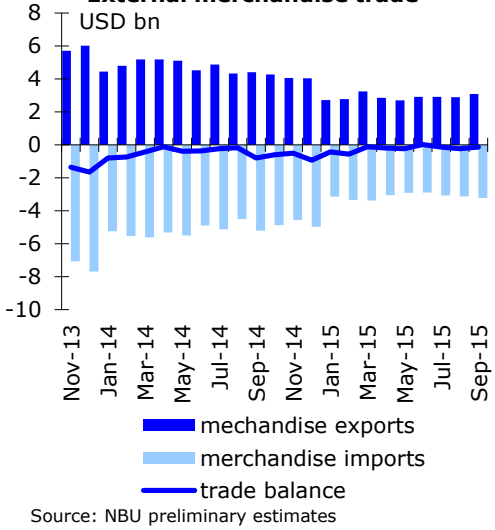
Source: Ukrstat

Balance of payments



Source: NBU preliminary estimates

External merchandise trade

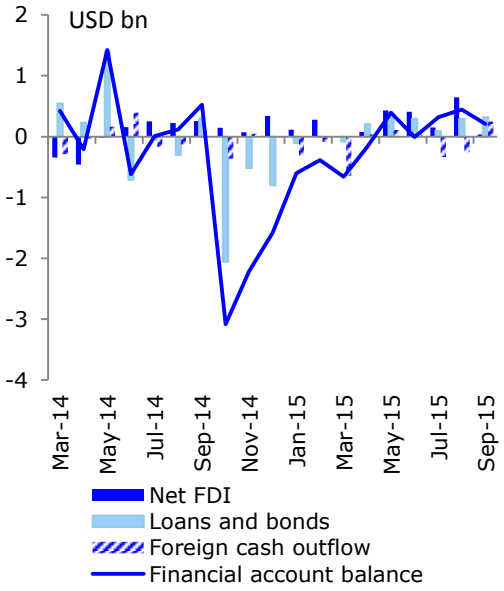


Source: NBU preliminary estimates

purchasing power of Ukrainians and import substitution. Termination of investment projects caused by restricted financing, higher costs of investment goods (due to hryvnia depreciation) and high economic and political uncertainty resulted in contraction of machinery imports by 17.4% yoy. Overall imports of manufactured products (including chemicals, wood, industrial goods, metals and machinery) decreased by 25.2% yoy. Imports of minerals decrease accelerated to 39.9% yoy due to statistical base effect. Imports of services declined by 16.4% yoy.

Financial account. Financial account surplus shrunk to USD 0.1 bn as net inflow of FDI dropped to less than USD 0.2 bn. The Government sector attracted another USD 0.5 bn of net external borrowings. External investment position of banks improved by USD 0.5 bn due to both increase in external assets as well as decrease in external liabilities. Investment position of real sector in September deteriorated by USD 0.4 bn, which included outflow of USD 0.4 bn of cash, net repayment of USD 0.2 bn of long-term loans and accumulation of USD 0.3 bn of trade loans. Amount of foreign cash outside banks shrunk by another USD 0.3 bn.

Financial account

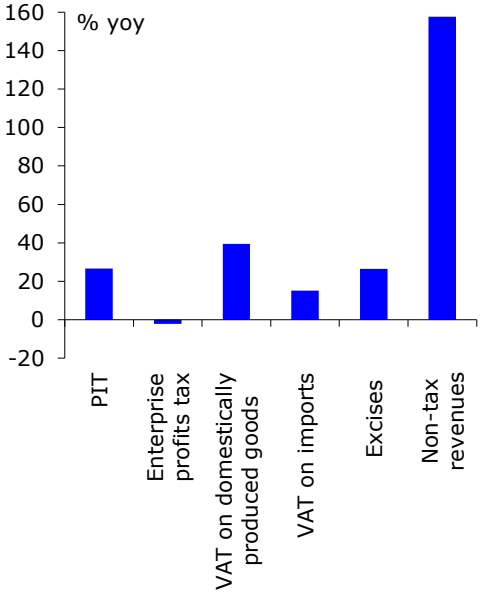


Source: NBU

Fiscal policy: Large fiscal surplus

Revenues. In September 2015 consolidated fiscal revenues increased by 49.1% yoy or UAH 18.5 bn as compared to September 2014. Temporary revenues from 5-10% of import duty surcharge explain 14.7% of this increase. Increase in wages as well as higher tax rate for passive income resulted in increase of PIT revenues by 26.6% yoy (or by UAH 1.8 bn). Revenues from excise duty increased by 26.5% yoy due to higher rates and inflation. At the same time, net VAT revenues grew by only 7.8% yoy as higher revenues from VAT from domestically produced goods and imports were almost counterweighted by surge in VAT refunds (attributed to hryvnia depreciation and higher exports in hryvnia equivalent). Non-tax revenues also increased. In particular, the NBU transferred profits at UAH 8.0 bn in September 2015 as compared to zero in the same months of last year.

Growth of Consolidated fiscal revenues in September 2015



Source: State Treasury reports

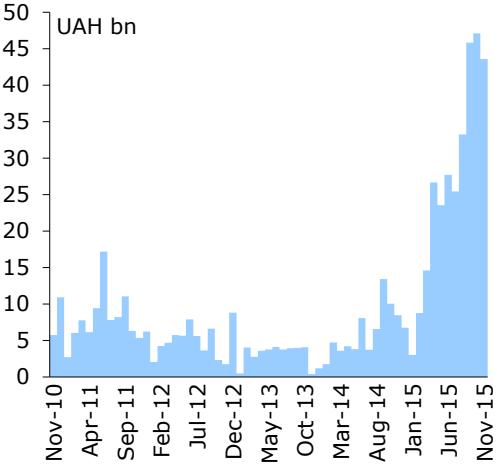
Execution rate. Revenues were still higher than planned. In particular, between January and September central fiscal revenues due to general fund were by 3.7% or UAH 13.0 bn higher than planned. At the same time, the expenditures were subject to procurement delays and planning delays. The Government also spent less than it expected on debt interest. Overall, fiscal expenditures (general fund) were by 7.9% or UAH 30.5 bn lower than the target. As usually, financing of social protection programs and intergovernmental transfers were financed the most and they were below the target by 2.4% and 3.4%, respectively.

Deficit. Higher than planned revenues, lower than planned debt and subsidy costs, delays in appropriating extra revenues resulted in the surplus of central government and local governments at UAH 8.8 bn and UAH 23.7 bn, respectively. As a result, the government funds at the Treasury surged to UAH 47.1 bn as of beginning of October.

Tax reform. The debates about tax reform continue. Members of the Rada Committee on Taxes and Custom and many other MPs have submitted their draft law on amendments to the Tax Code, which envisages rapid reduction of tax rates. In particular, the document suggests to reduce PIT rate to 10% (from current 15%-20%) and single social contribution rate to 20% (currently on average near 37%). Authors of the draft suggest that wage de-shadowing would offset some of the losses to the fiscal revenues and the Pension Fund. However, de-shadowing does not depend only on tax rate, but also on the trust to authorities and control mechanisms. The both are not present at the moment.

VAT rate is proposed at 15%, and VAT refunds are planned to fully automatic basis. This will likely result in lower net VAT revenues. EPT revenues are likely to drop due to suggested shift towards taxation of distributed income. At the same time, the Draft law suggests some simplification of tax administration, which is required to improve business climate. However, it also contains some questionable

Balance of the Single Treasury Account



* in the beginning of month
Source: State Treasury

provisions including introduction of excise duty invoices and re-introduction of fixed taxation of individual income without any accounting (for entrepreneurs with relatively small income).

Overall, the implementation of tax reform in this draft law is likely to result in fiscal gap of UAH 150-200 bn. This draft law in current form will likely be vetoed as it will increase fiscal deficit to levels not acceptable to the IMF. Derailment of the IMF program will increase risk that fragile macroeconomic stabilisation reached during recent months will be destroyed.

So far, the Ministry of Finance has not made public own draft on changes to the Tax Code. Publicly proposed concept of tax reform from the Ministry envisages shift towards flat tax rate for all major taxes – 20% for EPT, VAT, and PIT.

Social policy: Further simplification of subsidies procedure

Legislation. In September and October the Government further simplified the application for housing and utility subsidy. Now, households that rent apartment will have easier access to subsidies. Besides, the households will be able to provide information only on members that actually live in the apartment and not registered there without special inspection of such households. Income, which is taken into account while estimating eligibility for subsidy will not include compensation (including social assistance, charitable assistance and military wages) received by those, that took part in anti-terroristic operation in the East of Ukraine, and their families and payment received by individuals on election commissions. If families are eligible for subsidy only during heating period but applied beforehand, they will not be required to reapply for the subsidy. Besides, subsidies based on special circumstances (as decided by commission) will be extended automatically. Overall, all these changes are expected to result in further increase of number of families that receive subsidies.

Coverage. Between January and September the number of families that were granted housing and utility subsidy increased by 5.4 times to 2.6 million (17.7% of all households). Overall, spending on housing and utility subsidies reached near UAH 5.0 bn. Changes in the eligibility criteria for receiving subsidies (changed formula) resulted in wider demographics of subsidy recipients. Previously large part of subsidies was received by single pensioners (that had simplified eligibility for subsidy). Now, one-member family account for 47.7% of all households receiving subsidy (79.8% in the same period of 2014), while households with four and more members now account for 11.7% (2.1% last year). It might signal about higher coverage of poorer households with subsidies, as analysis indicates that in Ukraine often households with children are in higher risk of poverty.

Labour market: Recession continues

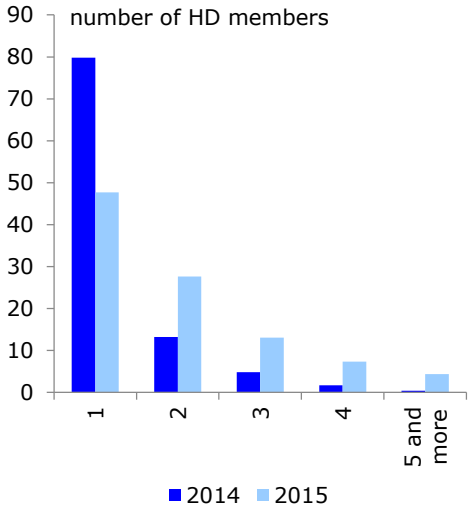
Wage. Average nominal wage in September grew by 24.8% yoy to UAH 4343. Real wage declined by 18.6% yoy as a result of bad financial results of companies, high inflation, and weak labour market.

Growth of nominal wage in agriculture accelerated to 28.5% yoy. This may be caused by the good harvest of wheat and wage indexation for inflation.

Industrial companies increased wages by 25.3% yoy, also likely due to wage indexation for inflation. Manufacturing companies increased their wages by near 30.0% yoy. The only outliers were textile industry (38.5% yoy increase), which benefited from import substitution and coke manufacturing and petroleum refinery (45.7% yoy increase) that benefited from high domestic demand on coke. At the same time, average wage increase in the electricity and gas supply sector was increased by only at 13.3% yoy likely due to unfavorable financial situation of companies in the sector.

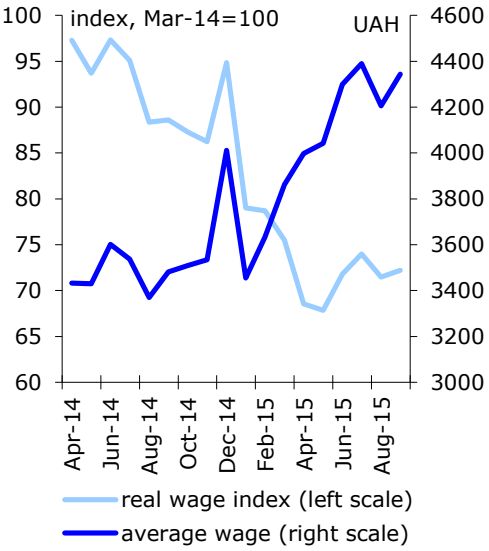
Basic wages in public sectors were frozen since 2014 and funds for bonuses and premiums were limited. As a result, wages increased by 18.7% yoy in public administration and defense, by 15.4% yoy and

Number of members in households with subsidies (Jan.-Sept.)



Source: Ukrstat

Average wage*



*not including AR Crimea
Source: Ukrstat

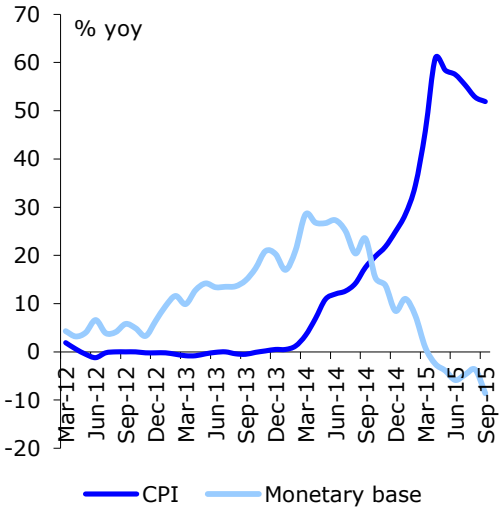
16.0% yoy in education and healthcare, respectively, due to indexation for inflation.

Monetary policy: Gas deflation

CPI in October fell by 1.3% mom and headline inflation slowed to 46.4% yoy. In October, the Ukrstat attempted to correct its previous overestimation of gas price increase in April (as it promised to the IMF). Overall, we estimate that the Ukrstat reduced CPI by over 3% in gas price adjustment. This is slightly less than we estimated in May but the revision will bring headline inflation much closer to real change in price level. Changes in regulated prices prevented CPI from falling more. In October, average 50% increase in heating tariff added about 0.9% to CPI and landline phone bill was increased by 15%. Prices for unprocessed food items on average increased by about 1.5% as prices were adjusted up or down in response to harvest results and seasonal patterns. For example Monthly core inflation was moderate at 0.8% mom but prices for a number of items increased by 1-3% reflecting substantial inflation expectations

In October, bank liquidity remained high but did not increase. NBU injected UAH 2 bn in liquidity through government bond purchases and UAH 5 bn through net purchases of foreign currency. The Government also reduced funds at the Single Treasury account by UAH 3.5 bn. Banks may have used added liquidity to fund increased demand for foreign currency observed in the end of October.

CPI and monetary base development



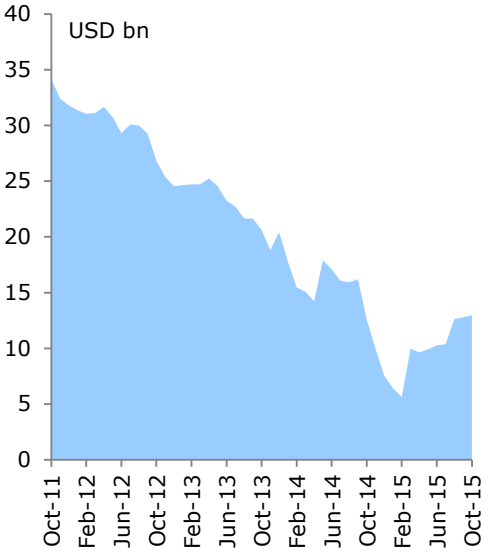
Source: Ukrstat, NBU

Exchange rate: Increased volatility

In October, interbank exchange rate remained in UAH 21-23 per USD range set by the NBU but it moved closer to upper end of the range by the end of the month. This may have happened as the NBU bought USD 300 m to increase international reserves and the Naftogaz purchased foreign currency for imported gas purchases. Seasonal increase in demand for imported consumer and investment goods may also have added to pressure on exchange rate. In the end of October, the NBU sold USD 40 m to keep exchange rate within the informal corridor.

Demand for the foreign currency was partially offset by seasonal increase in grain exports. Net sales of cash foreign currency to banks also remained positive at USD 105 m and NBU's international reserves reached USD 13.0 bn by the end of October.

NBU international reserves



Source: NBU

State debt: sovereign debt restructuring was finalised

Debt restructuring. In late October, the Ministry of Finance informed on finalization of sovereign debt restructuring. During bondholders meetings on October 14, the terms of the restructuring for 13 series (out of 14) of sovereign bonds were finally approved. The replacement of old bonds issue with new Eurobonds bonds due to approved debt restructuring terms is expected on November 12, 2015. Debt restructuring resulted in upgrade of Ukraine's ratings for obligations in foreign currency by key international sovereign rating agencies. In particular, the rating agency Standard & Poor's upgraded the rating from the level of selected default SD to comparatively high level of B- (which corresponds to the level of 2013).

Held by Russia the USD 3 bn Eurobond (maturing on December 20, 2015) did not became part of successful restructuring deal. Russia refused to accept common restructuring terms imposed on all other sovereign Eurobonds as it considered the debt as an official bilateral debt (not commercial), which should be paid in full without possibility of restructuring. The Ministry of Finance is likely to put moratorium on December's debt payment to Russia.

Tables

		Q3 13	Q4 13	Q1 14	Q2 14	Q3 14	Q4 14	Q1 15	Nov[c]	Dec[c]	Jan[c]	Feb[c]	Mar[c]	Apr[c]	May[c]	Jun[c]	Jul[c]	Aug[c]	Sep[c]	Oct[c]
Industrial production (real)	% yoy cum.	-5.2	-4.7	-5.0	-4.7	-8.6	-10.1	-21.4	-10.1	-10.7	-21.3	-21.7	-21.4	-21.5	-21.2	-20.5	-19.5	-18.0	-16.6	…
Construction (real)	% yoy cum.	-15.1	-14.5	-6.4	-8.9	-17.2	-19.3	-31.3	-19.3	-21.7	-36.7	-32.0	-31.3	-32.6	-38.5	-28.3	-26.7	-24.6	-22.8	…
Agricultural production (real)	% yoy cum.	3.0	13.7	6.0	-3.9	16.0	5.0	-4.7	5.0	2.8	-2.4	-3.6	-4.7	-4.8	-5.4	-9.3	-3.5	-5.8	-5.3	…
Retail trade turnover (real)	% yoy cum.	9.8	9.5	7.7	0.8	-5.3	-7.5	-23.9	-7.5	-8.6	-22.6	-21.2	-23.9	-25.3	-24.7	-24.6	-23.6	-23.1	-22.3	…
Average wage	UAH	3331	3390	3245	3488	3463	3508	3650	3534	4012	3455	3633	3863	3998	4042	4299	4390	4205	4343	…
CPI	% yoy eop	-0.5	0.5	3.4	12.0	17.5	21.8	45.8	21.8	24.9	28.5	34.5	45.8	60.9	58.4	57.5	55.3	52.8	51.9	46.4
PPI	% yoy eop	-0.9	1.7	3.9	15.9	26.9	32.8	51.7	32.8	31.8	34.1	41.0	51.7	48.6	42.0	37.9	37.0	33.0	32.5	30.2
Exports (USD)*	% yoy cum.	-6.2	-5.2	-7.7	-6.5	-9.8	-13.1	-32.9	-13.1	-15.0	-30.8	-32.3	-32.9	-34.5	-36.4	-35.4	-35.4	-34.6	-33.5	…
Imports (USD)*	% yoy cum.	-4.1	-3.4	-14.7	-18.6	-24.5	-27.1	-36.0	-27.1	-27.8	-36.3	-35.9	-36.0	-37.2	-39.3	-39.2	-38.8	-36.4	-36.2	…
Merchandise trade balance	USD bn cum.	-14.2	-19.6	-1.9	-0.6	-5.2	-6.5	-1.0	-6.5	-7.6	-0.4	-0.9	-1.0	-1.1	-1.3	-1.2	-1.4	-1.9	-2.0	…
Current account**	USD bn cum.	-11.4	-16.4	-1.3	-0.6	-3.8	-4.6	-0.5	-4.6	-5.3	-0.3	-0.6	-0.5	-0.3	-0.3	0.0	0.1	-0.1	0.0	…
Gross international reserves	USD bn eop	21.6	20.4	15.1	17.1	16.4	7.5	10.0	10.0	7.5	6.4	5.6	10.0	9.6	9.9	10.3	10.4	12.6	12.8	13.0
Monetary Base	% yoy eop	14.8	20.3	28.5	25.1	23.5	13.8	0.9	13.8	8.5	11.0	7.5	0.9	-2.5	-3.9	-5.9	-4.7	-3.7	-8.6	…
Lending rate on UAH credits	% pa, aop	15.3	16.5	18.5	17.5	16.4	16.4	19.9	16.7	16.9	17.2	18.8	23.6	23.8	23.6	22.0	21.2	21.2	21.0	…
Exchange rate (interbank)	USD aop	8.15	8.21	9.1	11.71	12.58	13.56	21.23	14.75	15.63	15.94	24.77	22.98	22.49	20.94	21.26	21.79	21.65	21.79	21.94
Exchange rate (official)	USD aop	7.99	7.99	8.9	12.71	12.58	13.56	21.18	14.70	15.62	15.81	24.48	23.26	22.71	20.92	21.23	21.76	21.54	21.78	21.84
Exchange rate (official)	EUR aop	10.58	10.87	12.14	13.71	16.67	17.21	23.88	18.36	19.26	18.53	27.78	25.32	24.47	23.32	23.84	23.94	23.93	24.46	24.56

Sources: Ukrstat, NBU, 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. Since 2015 the Ukrstat also does not include data for occupied territories in the East of Ukraine

Key Economic Indicators		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014[c]
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	1566.7
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	132.0
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	-6.8
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	-10.7
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	2.8
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	12.1
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	24.9
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	17.1
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	31.8
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	-0.2
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	-0.3
Current account	USD bn	1.5	1.4	3.1	2.9	6.9	2.5	-1.6	-5.3	-12.9	-1.9	-2.9	-9.3	-14.3	-16.4	-5.3
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	-4.0
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	0.3
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	7.5
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	-4.6
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	39.9	70.2
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	39.0
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	8.5
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	11.87
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	15.77
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	15.72
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	19.26

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

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

[c] Data excludes Crimea

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		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[c]	Q2 14[c]	Q3 14[c]	Q4 14[c]	Q1 15[c]	Q2 15[c]
GDP	UAH bn	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	313.6	375.9	434.2	443.1	367.6	449.6
GDP (real)	% yoy	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	-1.2	-4.5	-5.4	-14.8	-17.6	-14.6
Household consumption (real)	% yoy	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	2.2	-9.0	-15.5	-13.6	-20.7	-27.6
State consumption (real)	% yoy	-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	-6.0	4.5	-0.5	3.5	5.0	-6.7
Gross fixed capital formation (real)	% yoy	-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	-19.9	-16.8	-26.7	-26.2	-25.1	-13.8
Exports of goods and services (real)	% yoy	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	-5.8	-2.6	-16.8	-31.0	-26.2	-22.5
Imports of goods and services (real)	% yoy	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	-13.0	-11.1	-31.9	-29.0	-20.1	-32.2
Agriculture, hunting, forestry (real)*	% yoy	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	5.9	-9.0	25.7	-19.1	-4.8	-11.7
Manufacturing industry (real)*	% yoy	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	-8.8	-8.0	-14.8	-16.7	-25.6	-21.8
Construction (real)*	% yoy	-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	4.4	-16.7	-24.1	-30.9	-35.3	-25.6
Trade, repair services (real)*	% yoy	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	-3.2	-8.2	-17.5	-21.7	-24.8	-20.4
Transport (real)*	% yoy	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	-2.3	-5.9	-5.6	-12.1	-13.2	-2.7
Balance of payments																				
Current account balance	USD bn	0.5	-1.6	-1.7	-2.6	-4.3	-1.9	-3.7	-3.9	-4.8	-3.2	-2.3	-6.0	-5.0	-1.3	-0.8	-1.2	-1.4	-0.5	0.3
Current account balance	% of GDP	1.6	-4.9	-4.4	-5.6	-9.5	-5.2	-8.5	-8.1	-10.1	-8.5	-5.1	-12.2	-9.9	-3.6	-2.6	-3.4	-6.7	-3.1	1.3
Trade balance in goods	USD m	-978	-3951	-3211	-5098	-5771	-4292	-5818	-5503	-6233	-4635	-3677	-7881	-5935	-2195	-1185	-1412	-2336	-1104	-389
Trade balance in services	USD m	1392	1614	1882	2523	1867	1864	1697	2361	1578	1349	1504	2575	1066	937	443	456	686	633	469
Current transfers	USD m	728	1039	878	988	803	683	805	777	711	533	589	480	547	241	494	306	500	443	592
Direct investment (FDI)	USD m	1196	880	2422	2090	1623	1663	1091	2002	1871	821	472	1199	859	-665	-319	725	558	460	909
Portfolio investments (equity)	USD m	-18	149	113	42	207	-3	74	83	339	705	579	664	-757	-239	-50	-84	-17	-13	…
Gross international reserves	USD bn	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	7.5	10.0	10.26
Exchange rate (interbank), UAH/USD	aop	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	13.56	21.23	21.26
Exchange rate (official), UAH/USD	aop	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	21.18	21.33	21.23
Fiscal indicators																				
Consolidated fiscal revenues	% of GDP	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	29.9	25.1	27.7	38.2	60.4
Personal income tax	% of GDP	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	4.3	5.1	5.6	9.2
Enterprise profits tax	% of GDP	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	1.9	1.6	4.5	2.8
Value-added tax	% of GDP	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	6.9	10.2	11.7	16.3
Excise tax	% of GDP	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	3.1	2.8	3.4	6.0
Consolidated fiscal expenditures	% of GDP	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	35.6	35.3	27.6	35.9	34.3	57.1
Current expenditures	% of GDP	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	35.1	34.3	26.1	33.9	32.5	54.3
Capital expenditures	% of GDP	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	1.5	1.9	1.8	2.8
Consolidated fiscal balance	% of GDP	-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	-5.4	-2.8	-8.8	3.8	3.2
Privatisation receipts	% of GDP	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	0.1	0.0	0.0
Labour market																				
Average wage (real)	% yoy	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	-11.0	-13.4	-20.1	-27.8
Household income (real)	% yoy	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	-3.4	-6.8	-5.6	-19.2	-23.5	-34.0
Unemployment rate (ILO methodology)	% cum	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	9.0	8.2	9.5	10.6	9.6	8.8
Banking system																				
Monetary aggregate M0	% yoy cum	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	19.0	6.0	-1.3
Monetary aggregate M2	% yoy cum	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	14.2	5.4	9.0	3.1
Household deposits in national currency	% yoy cum	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	-22.1	-19.1	-17.7
Household deposits in foreign currency	% yoy cum	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	18.0	25.4	11.6
Com. bank credits in national currency	% yoy cum	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	-9.1	-11.0	-11.1
Com. bank credits in foreign currency	% yoy cum	-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	53.5	58.4	27.7
Long-term com. bank credits	% yoy cum	-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	21.7	17.9	3.1
Long-term com. bank credits	% of total	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	59.5	58.5	57.6
Average lending rate on national currency credits	% p.a.	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	16.6	19.9	23.1
Average lending rate on foreign currency credits	% p.a.	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	8.8	8.2	9.3

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 balan

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