

April 2019
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Executive Summary

- ❖ Ukraine successfully completed the first round of the presidential elections on March 31. The rate of participation in the first round was high and reached 63%. The elections were regarded by international observers as fair and transparent. As was expected, comedian and actor Volodymyr Zelenskiy received the highest number of votes (about 30%) while current President Poroshenko was second with about 16% of the votes. The second round of the elections between these two presidential candidates will take place on April 21st. The current polls give Zelenskiy a 2:1 advantage.
- ❖ Despite election uncertainties, in February 2019 the Ukrainian economy continued to perform well supported by strong domestic demand. In fact, high-frequency data for February show high rates of growth in construction activities (19.5% yoy), followed by retail trade turnover (6.8% yoy), and by agricultural output (3.6% yoy.) In addition, transportation and passenger trade turnover expanded by 2.7% yoy and 3.9% yoy, respectively. At the same time, Ukrainian industrial production declined at a lower rate of -1.8% yoy in February, compared to -3.3% yoy, in January 2019. GDP is now expected to grow by 2.8% in 2019.
- ❖ Following a fiscal deficit in January, the consolidated budget returned to surplus in February. The cumulative consolidated budget balance from the beginning of the year amounted to at UAH 4.7 billion in January-February.
- ❖ In February, consumer inflation continued to decelerate. The all items index dropped 0.4 percentage points to 8.8% yoy. Inflation is expected to decline further to 8% by the end of the year.
- ❖ National currency bank deposits continue to improve in February. National currency deposits by the corporate and household sectors grew at rates of 10.6% yoy and 15.0% yoy, respectively.
- ❖ The UAH/USD exchange rate appreciated at the beginning of March, then remained relatively stable, and finally depreciated slightly by the end of the month. Overall, the UAH/USD exchange rate depreciated by 1.6% in March to 27.2 UAH/USD.
- ❖ In February 2019, the current account of the balance of payments had a deficit of USD 381 million, due to a higher growth in imports of goods (15% yoy to USD 4.6 billion), than in goods exports, which increased by 7.3% yoy (to USD 3.6 billion). This deficit was partly covered by foreign inflows of USD 130 million, principally from foreign direct investments. International reserves declined slightly to about USD 20 billion.

Main Macroeconomic Indicators	2013	2014	2015	2016	2017	2018	2019f
<i>GDP, USD billion</i>	180	130	87	93.4	113	125	135
<i>Real GDP Growth, % yoy</i>	0.0	-6.6	-9.9	2.4	2.5	3.3	2.8
<i>Fiscal Balance (incl. Naftogaz/Pension Fund), % of GDP</i>	-6.5	-11.7	-2.1	-2.3	-1.4	-1.9	-2.3
<i>Public Debt, External and Domestic, % of GDP</i>	40.4	69.4	79.1	80.9	71.8	62.6	64.5
<i>Consumer Inflation, eop, % yoy</i>	0.5	24.9	43.3	12.4	13.7	9.8	8.0
<i>NBU Key Policy Interest Rate, % eop</i>	6.5	14.0	22.0	14.0	14.5	18.0	16.0
<i>Hryvnia Exchange Rate per USD, eop</i>	8.2	15.8	24.0	27.1	28.1	27.7	30.0
<i>Current Account Balance, % of GDP</i>	-9.2	-3.5	1.8	-1.5	-2.2	-3.7	-3.0
<i>Merchandise Exports, USD billions</i>	59	51	35	34	40	43	46
<i>Merchandise Imports, USD billions</i>	81	58	39	40	49	56	58
<i>FDI, Net Annual Inflow, USD billion</i>	4.5	0.4	3.0	3.3	2.3	2.4	2.0
<i>International Reserves, USD billion</i>	20.4	7.5	13.3	15.5	18.8	20.8	18.0
<i>Public External Debt, USD billion</i>	31.7	34.9	42.6	42.5	47.0	49.9	50.0
<i>Private External Debt, USD billion</i>	110.3	91.2	76.0	69.9	70.0	71.0	72.0

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Political and Reform Developments

Ukraine successfully completed the first round of presidential elections on March 31. The rate of participation in the first round was high and reached 63%. As was expected, comedian and actor Volodymyr Zelenskiy received the highest number of votes (about 30%) while current President Poroshenko was second with about 16% of the votes. President Poroshenko's poor performance has been partly attributed to a slowdown in the speed of reforms in the last two years and a number of recent corruption scandals, which became publicly available several weeks before the elections. Yulia Tymoshenko, who was one of the leaders of the presidential polls throughout the campaign, received only about 13% of the votes and was not able to secure a place in the second election round. Her low result was unexpected for Tymoshenko and her supporters. Tymoshenko's office issued a statement accepting the results and stating that it would start preparation for the upcoming parliamentary elections, which are scheduled for October 27.

Although the official results of the first round would be announced only on April 15, and the second round of the elections is scheduled for April 21st, the campaign has already become very intensive. Both candidates are expected to have public debates on April 19th. The place for the debate was defined according to suggestion of Volodymyr Zelenskiy as a National Stadium, which is able to host up to 70 thousand people. This format of debates is a new one not only for Ukraine but for many other countries as well.

The elections have been regarded by international observers as fair and transparent. Together with the high level of openness of the candidates and their wiliness to go to public is evidence that Ukraine has become an irreversible democracy. Moreover, the economic programs of the two candidates are clearly pro-west and it is very likely that after the elections the country will be able to accelerate implementation of the reform agenda, which was slowed down for some time. Despite of the outcome of the presidential elections Ukraine will continue with its Euro and Euro-Atlantic course as it was already proclaimed by both candidates.

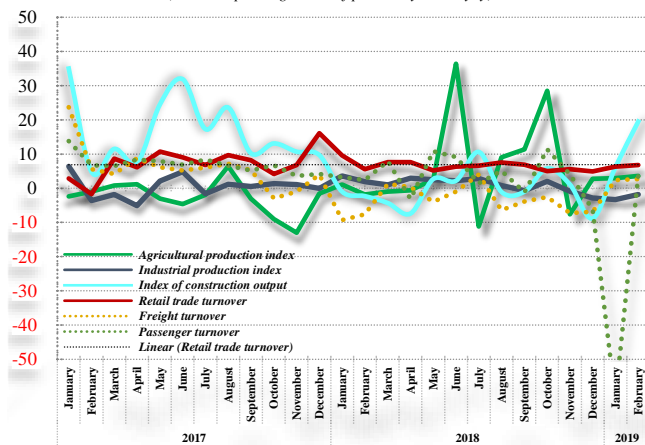
Economic Growth

Despite election uncertainties, in February 2019 the Ukrainian economy continued to perform well in almost all sectors, supported by strong domestic demand. In fact, high-frequency data for February show high rates of growth in construction activities (19.5% yoy), followed by retail trade turnover (6.8% yoy), and by agricultural output (3.6% yoy.) In addition, transportation and passenger trade turnover expanded by 2.7% yoy and 3.9% yoy, respectively. At the same time, Ukrainian industrial production declined at a lower rate of -1.8% yoy, compared to -3.3% yoy, in January 2019. Given the poor performance of industrial activities, GDP for 2019 is likely to be only around 2.8%.

Within the industrial sector, in February 2019 three subsectors showed good performance, i.e., the pharmaceutical goods industry (by 23.1% yoy), rubber and plastic manufacture (by 4.6% yoy), and foodstuffs and beverages (by 0.6% yoy). The electricity, gas, steam and air conditioning supply sector also had growth of 1.3% yoy, in February 2019.

Economic Performance of Ukraine by Sector

(To corresponding month of previous year, % yoy)



Source: State Statistics Service, the Bleyzer Foundation

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Other manufacturing subsectors had negative results as follows: chemicals & chemical products (-19.5% yoy); textile industry, sewing of clothes, leather & leather articles (-4.6% yoy); wood products, paper & printing (-7.3% yoy); furniture, other repair (-6.1% yoy); machinery and equipment (-4.3% yoy); basic metals and fabricated metal products (-3.7% yoy); and coke & refined petroleum products (-2.1% yoy).

From a geographical point of view, the major improvements of industrial output of Ukraine took place in the following oblasts: Rivne (17.3% yoy), Vinnytsya (9.3% yoy), Zakarpattia (3.6% yoy), Chernivtsi (3.1% yoy), Ternopil (2.3% yoy), Donetsk (1.9% yoy), Poltava (1.9% yoy), Cherkasy (1.5% yoy), and Kyiv city (1% yoy).

Other regions showed production reductions in February 2019 with estimated declines in output as follows: Khmelnytskyi (-17.7% yoy), Chernihiv (-8.8% yoy), Lviv (-8.2% yoy), Ivano-Frankivsk (-7.6% yoy), Zhytomyr (-6.5% yoy), Sumy (-6.4% yoy), Kirovohrad (-5.9% yoy), Kharkiv (-5.2% yoy), Volyn (-4.7% yoy), Odessa (-4.0% yoy), Zaporizhzhya (-3.4% yoy), Mikolayiv (-2.4% yoy), Luhansk (-2% yoy), Kyiv (-0.8% yoy), and Dnipropetrovsk (-0.4% yoy).

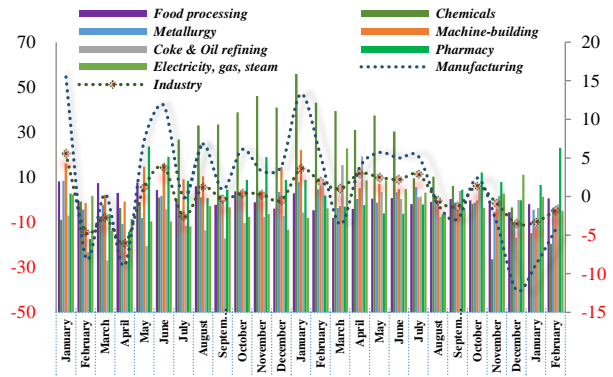
Fiscal Policy

Following a fiscal deficit in January, the consolidated budget returned to surplus in February. This was the result of improved performance of fiscal revenues and slower growth of expenditures. The cumulative surplus of local budgets of UAH 6.9 billion more than offset a deficit of UAH 1.8 billion in the state budget. Thanks to accelerated growth in budget revenues, the government was more active in repaying previously taken loans. Net repayments reached UAH 11.7 billion. However, those repayment were partially covered by liquidity regulation instruments and cash resources additionally issued by the government. The cumulative consolidated budget balance from the beginning of the year was positive at UAH 4.7 billion in January-February.

Consolidated fiscal budget revenues returned to growth in February. Furthermore, they grew at high rate of 23.7% yoy. This growth was ensured by tax revenues, while growth of nontax revenues significantly decelerated (from 21.9% yoy to 2.8% yoy). The growth of tax revenues was driven by higher receipts from both domestic taxes and receipts from taxes on imported goods. Receipts from personal income tax continue to grow at high rate (23.1% yoy), while growth of corporate profit tax receipts turned negative (7.4% yoy) because of negative developments at the local level. Cumulative consolidated budget revenues

Industrial Production by Sectors, % yoy

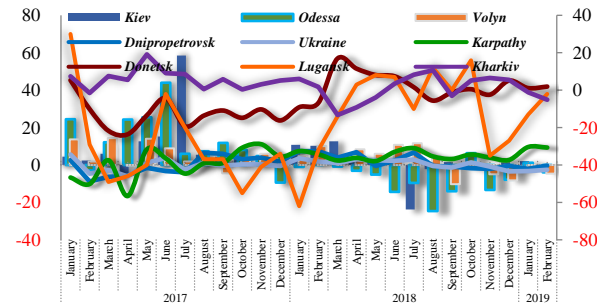
(To corresponding month of previous year)



Source: The Bleyzer Foundation

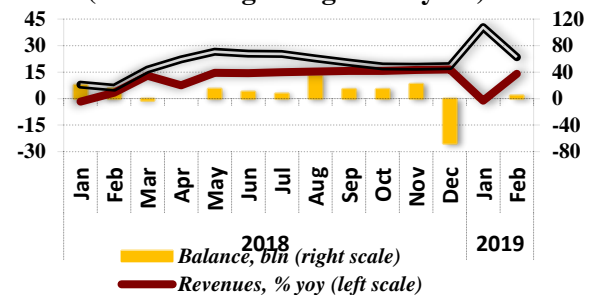
Industrial Production by Regions, % yoy

(To corresponding month of previous year)



Source: The Bleyzer Foundation

Dynamics of Consolidated Budget Components (from the beginning of the year)



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

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grew by 14.0% yoy over the first two months of the year.

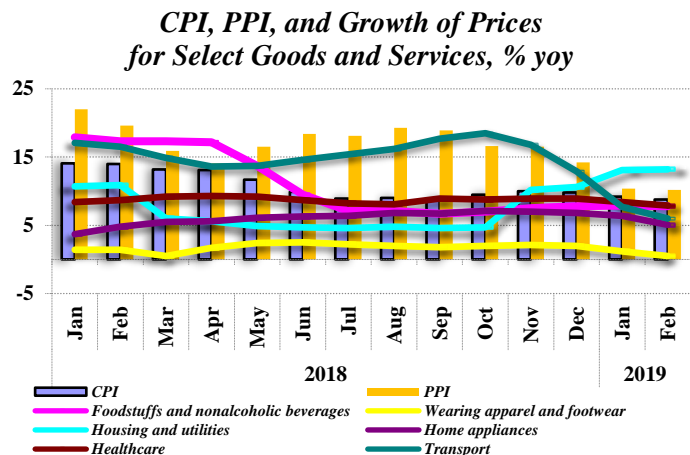
The growth of consolidated budget expenditures significantly decelerated in February. It declined by almost five times to 9.4% yoy, mainly because of lower social security expenditures. Growth of payroll expenditures and expenditures on goods and services remained relatively high (19.8% yoy and 11.2% yoy, respectively). Growth of capital expenditures decreased by more than three times to 21.3% yoy. Cumulative consolidated budget expenditures from the beginning of the year reached 23.4% yoy by the end of February.

Principal and servicing payments on state and guaranteed debt denominated in foreign currency further increased in February. Total payments equaled USD 1.3 billion equivalent. Servicing payments and repayment of sovereign bonds and other foreign currency liabilities totaled USD 837.8 million equivalent. In addition, USD 447.6 million equivalent was paid by the government and the NBU to the IMF.

Monetary Policy

Inflation. In February consumer inflation continued to decelerate. The all items index dropped 0.4 percentage points to 8.8% yoy. Core inflation decelerated even faster from 8.3% yoy to 7.8% yoy. The effect of the exchange rate appreciation more than offset temporary faster growth of foodstuffs prices.

Most major groups of goods and services saw little or no changes in price dynamics. Communication services were the only major group reporting significant acceleration in price growth (by 0.9 percentage points to 15.7% yoy). Notable deceleration in price growth was reported for transport (by 1.7 percentage points to 6.0% yoy), home appliances (by 1.3 percentage points to 5.1% yoy), and footwear and wearing apparel (by 0.7 percentage points to 0.5% yoy).



Source: State Statistical Service of Ukraine, The Bleyzer Foundation

Taking into account current consumer inflation dynamics and common seasonal inflation trends, we expect consumer inflation to end the year at around 8.0% yoy.

Banking Sector. The situation with bank deposits improved in February. National currency deposits grew at a rate close to that observed in January as both corporate and household sectors reported similar growth (10.6% yoy and 15.0% yoy respectively). The decline in foreign currency deposits decelerated a bit. The mentioned changes were the result of further increases in wages, high profitability of the national currency deposits and increased foreign currency inflows as compared to January.

By contrast, bank lending activities were weak in February. High growth of household national currency loans was almost fully offset by the decline of correspondent corporate loans because of lower business activity common for the month.

Further declines in cash resources led to deceleration of the monetary base growth to 4.5% yoy. At the same time, money supply expanded at an accelerated rate of 7.3% yoy, on the back of fast growth in the national currency deposits and slower decline in foreign currency deposits.

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Hryvnia Exchange Rate. The UAH/USD exchange rate dynamics sustained several trend changes in March. The exchange rate gradually appreciated at the beginning of the month thanks to the placement of domestic sovereign bonds denominated in national currency. High profitability of bonds attracted many non-residents who had to sell foreign currency at the interbank forex market to pay for bonds. Then, Ukrzaliznytsia started active purchases of dollars for bond repayment purposes on March 12th. The company had to repay USD 175 million, which is a large amount for the currently thin interbank forex market. Thus, the exchange rate reversed the trend. Furthermore, depreciation accelerated in the upcoming days because of speculators and exporters, who started limiting dollar supply to increase profits. The situation stabilized on March 21st, and the exchange rate even appreciated back a bit. However, VAT reimbursements led to increase in hryvnia resources and increased pressure on hryvnia at the end of the month, causing another wave of depreciation. Overall, the UAH/USD exchange rate depreciated by 1.6% in March.

Official UAH/USD Exchange Rate (based on the Average Weighted Rate at the Interbank Forex Market)

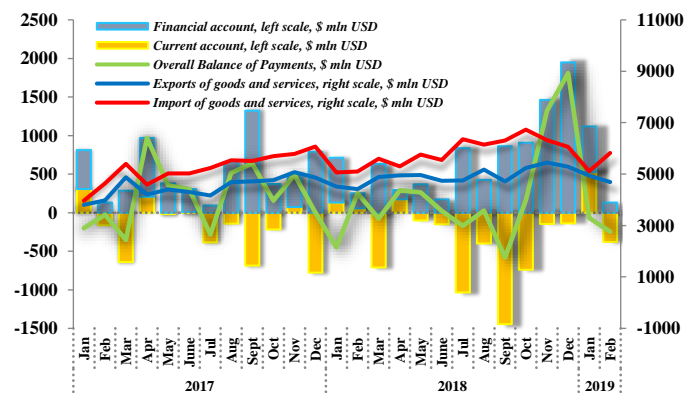


Source: The NBU. The Bleyzer Foundation

International Trade and Capital

According to the NBU, in February 2018, the current account of the balance of payments had a deficit of USD 381 million, compared to a surplus of USD 56 million in February 2018. The current account deficit was due to a higher growth in imports of goods (15% yoy to USD 4.6 billion), than in goods exports, which increased by 7.3% yoy (to USD 3.6 billion). The primary income account (employees' compensation and investment income) had a surplus of USD 500 million in February. The secondary income account (principally foreign personal transfers) also had a surplus of USD 242 million in the month.

Ukraine's External Balance of Payments



Source: NBU, the Bleyzer Foundation

Ukrainian exports continue to be dominated by agricultural exports, which amounted to USD 1,724 million in February (representing 48% of total exports and had a growth rate of 27% yoy). Metallurgical exports represent the second largest export group (about USD790 million in February), but had an 18% yoy decline compared to February 2018. Exports of mineral products amounted to USD 317 million in February, showing a growth rate of 5% yoy. Exports of machinery and equipment reached USD 240 million, with a growth rate of 15% yoy.

From a geographical point of view, in January-February 2019 Ukraine exports to Russia amounted to USD 361 million and fell by 20% yoy. They now represent 4.9% of total exports, compared to 6.7% in January-February 2018. Exports to Asia increased by 7.3% yoy, representing 30.5% of the total Ukrainian exports. Exports to

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Europe increased by 6.6% yoy and now account for 40% of exports. Exports to the US increased by 55% yoy, but are still small at 3% of total exports.

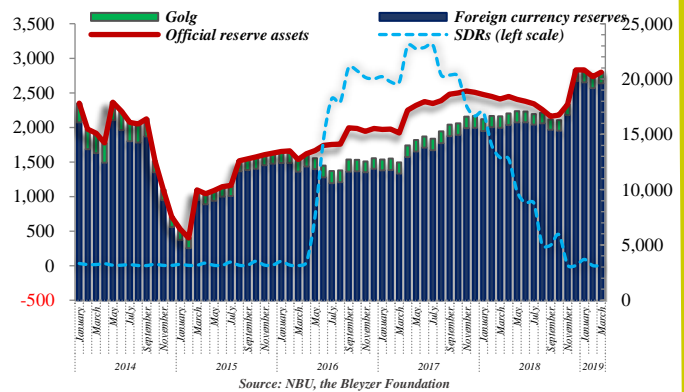
With regard to merchandise imports, in February 2019, machinery and equipment accounted for the major share (33% of the total import amount, or USD 1,500 million). The second largest imports category was chemical products, which accounted for 20% of the total imports (USD 928 million), increasing by 5.6% yoy. Imports of mineral products (including energy) are the third largest import category, increasing by 13.8% yoy to USD 872 million. Agricultural imports represent the fourth largest import group (with 10.3% of the total at USD 481 million) and increased by 5.3% yoy in February.

Geographically, Europe is the largest supplier of goods to Ukraine, with a 41% share of January-February imports. It was followed by Asia with a 24.2% share. The share of Russia in Ukrainian imports has been reduced to 13.2% of the total, compared to 17.3% in January 2018.

In February 2019, the financial account had net inflows of USD 131 million. The largest inflows came from foreign direct investments, which reached USD 369 million in February, and were directed mainly to the corporate sector. The major outflows were due to heavy debt repayments by commercial banks.

The inflows in the financial account (USD 131 million) were insufficient to cover the current account deficit of USD 381 million and the overall balance of payments had a small deficit of USD 250 million in February, slightly lowering international reserves to about USD 20 billion as of the beginning of March.

Ukraine's International Reserves, mln USD



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