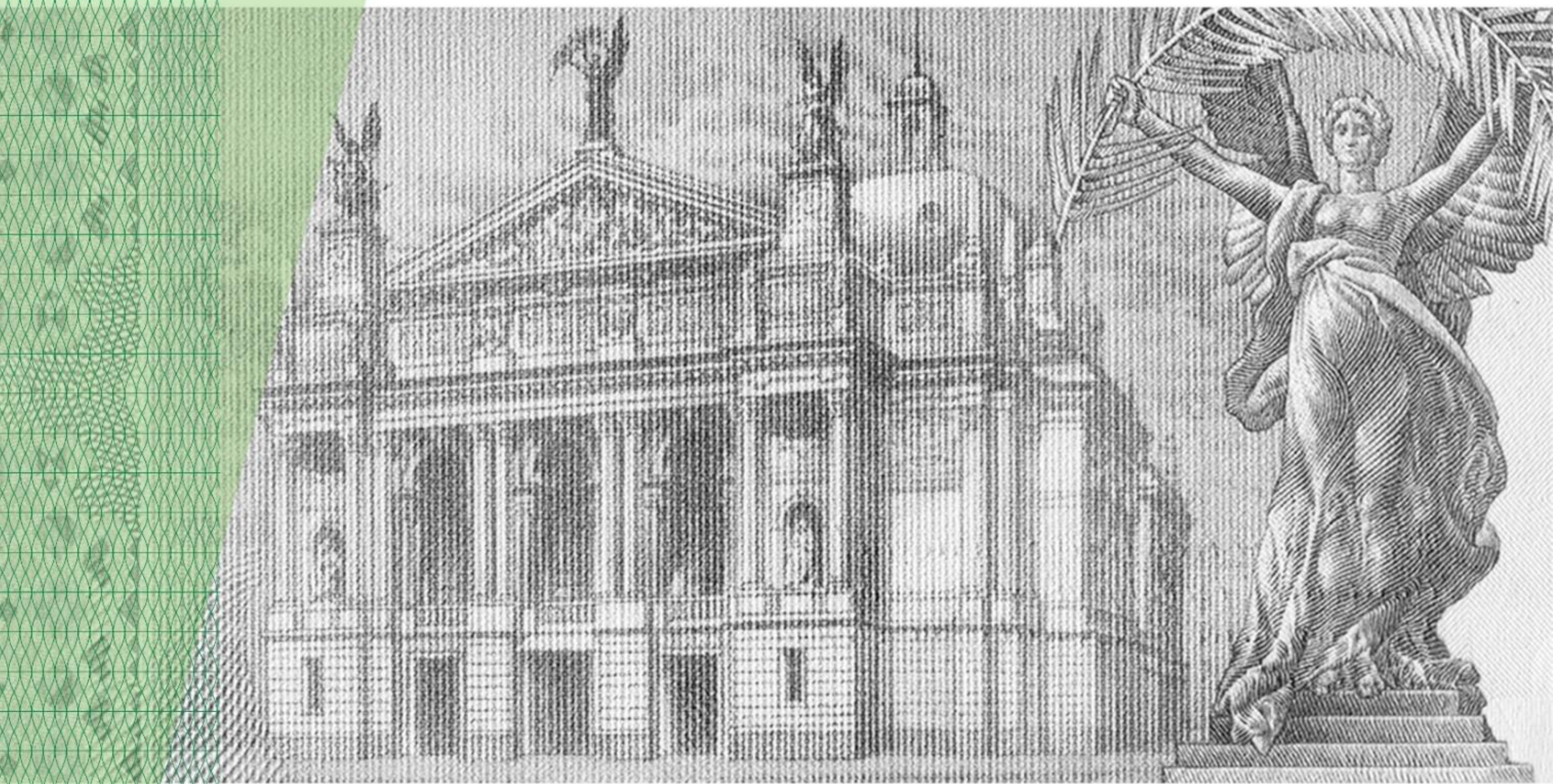
National Bank of Ukraine

Inflation Report

January 2025

Summary



Despite the challenges of full-scale war, the NBU remains committed to its mandate to preserve price and financial stability – the key to achieving sustainable economic recovery. At the current stage, price stability is being delivered through the use of a flexible inflation targeting regime and a consistent combination of interest-rate-policy and exchange-rate-policy instruments, along with FX restrictions applied in accordance with the *Monetary Policy Guidelines for the Medium Term* and *the Strategy for easing FX restrictions, transition to greater exchange rate flexibility and return to inflation targeting*.

In particular, monetary policy aims to bring inflation, measured by the yoy change in the CPI, to its target of 5% over the relevant policy horizon, which does not exceed three years. The flexibility of the current monetary regime allows moderate and relatively short-term deviations of inflation from its quantitative target due to domestic and external factors. On the one hand, such an approach helps the Ukrainian economy adapt to shocks and supports its recovery, and, on the other hand, it allows inflation expectations to be kept under control.

The NBU is taking steps to strengthen the effectiveness of monetary transmission channels and to continue to restore the key policy rate's function as a monetary instrument. Changes in the key policy rate and adjustments to the operational framework of interest rate policy take into account significant shifts in the balance of risks and are primarily aimed at maintaining the sustainability of the FX market and ensuring price stability.

Sticking to the principles of managed flexibility of the exchange rate, the NBU maintains an active presence in the FX market and compensates for any structural shortage of foreign currency in the private sector. This ensures that the exchange rate fluctuates moderately in both directions as market conditions change. Coupled with smoothing out excessive exchange rate volatility, this also contributes to keeping inflation and exchange-rate expectations in check, maintaining confidence in the hryvnia and bringing inflation to the target of 5%. Concurrently, exchange rate flexibility makes it possible to fortify the Ukrainian economy's and the FX market's resilience to domestic and external shocks, as well as reducing the risk of accumulation of external trade imbalances.

Aware of the urgent need to minimize FX market distortions, the NBU is gradually easing the FX restrictions as appropriate prerequisites are met. This will improve the conditions for doing business in Ukraine, and for the entry of domestic businesses into new markets. It will also support the economy's recovery and promote new investment inflows into the country.

The NBU plans to use flexible inflation targeting until the economy resumes normal functioning and inflation targeting is restored to its full format, with a floating exchange rate.

The analysis in the current Inflation Report (January 2025) is based on the data available at the date of its preparation. Thus, the time horizon of the analysis may vary for some indicators. For the majority of indicators, the cut-off date for the data in this report is 22 January 2025. The Inflation Report presents the forecast for the country's economic development in 2025–2027 that was prepared by the Monetary Policy and Economic Analysis Department and approved by the NBU Board at its monetary policy meeting on 23 January 2025[1].

The NBU Board makes decisions on the key policy rate and other monetary instruments in line with a schedule published in advance. The decisions the NBU Board makes in January, April, July, and October are based on the latest macroeconomic forecast. At the remaining four meetings (in March, June, September, and December), the NBU Board makes its decisions based on assessments of risks and uncertainty that take into account the economic developments in Ukraine and abroad since the last forecast. The decisions are announced at a press briefing held at 2 p.m., after the NBU Board's monetary policy meeting. A press release that reflects the NBU Board's consensus perspective on its decisions is published at the same time. The summary of the discussion at the Monetary Policy Committee is published on the 11th day after the decision is taken. The summary shows the depersonalized opinions of all MPC members on the optimal monetary policy decisions to be made. It includes differences of opinion and the reasoning behind them.

Previous issues and presentations of the Inflation Report, the forecast of the main macroeconomic indicators, and data in tables and figures are available here.

[1] NBU Board decision No. 25 *On Approval of the Inflation Report* dated 23 January 2025.

Summary

The baseline scenario of the NBU's macroeconomic forecast assumes that Ukraine will continue to conduct prudent monetary and fiscal policies aiming at maintaining macrofinancial stability, and will consistently meet its commitments under programs with international partners, which will keep providing sufficient financial support. The NBU assumes that conditions in which the economy operates will gradually normalize over the forecast horizon. This will take the form of the full unblocking of seaports, the expansion of opportunities for investment and economic activity, and the gradual return of forced migrants to Ukraine.

Inflation reached 12% in 2024, and pressure on prices persists in early 2025

In December 2024, inflation accelerated to 12% yoy, exceeding the NBU's previous forecast (October 2024 Inflation Report). According to the NBU's estimates, inflation continued to rise in January.

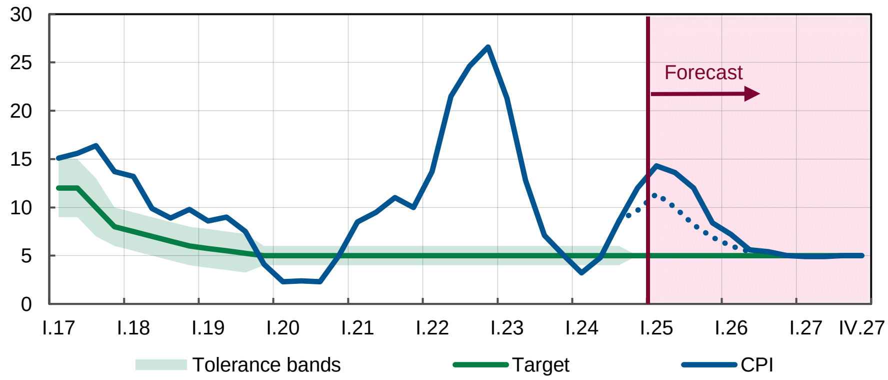
The rapid growth in consumer prices was to a large extent driven by temporary factors, primarily the ones related to effects of last year's weaker harvests. At the same time, underlying price pressures also increased. This was evidenced by the continued acceleration of core inflation (to 10.7% yoy in December), in particular due to a sharp rise in services prices (12.5% yoy in December). These price dynamics were driven by businesses' higher expenses on raw inputs, materials, and electricity, as well as by wage increases against the backdrop of persisting staff shortages. That said, in recent months, price growth has been somewhat restrained by a strengthening of the UAH/EUR exchange rate, which is important for Ukrainian imports.

Inflation reaching double digits is negatively affecting the inflation expectations of households and businesses. Nevertheless, the expectations of financial analysts and banks remain relatively sustainable.

Thanks to the waning of temporary factors behind the price pressure and the NBU's interest rate and exchange rate policy measures, inflation will decline to 8.4% in 2025 and reach the 5% target in 2026

In the first months of 2025, inflation is likely to continue to rise due to the persistent impact of both temporary factors – including the effects of last year's lower harvests – and underlying drivers – among them pressure from businesses' production costs. Inflation will peak in Q2 and will start to decline from the middle of the year.

Figure 1.[2] **CPI change (end of period, % yoy) and inflation targets**



Source: SSSU, NBU staff estimates.

Inflation is expected to slow to 8.4% at the end of 2025 and to reach the target of 5% in 2026. The NBU's interest rate and exchange rate policy measures, as well as stronger

[2] Unless specified otherwise, a dashed line in the figures indicates the previous forecast.

harvests, improved energy supply, a narrower fiscal deficit, and subdued external price pressures will contribute to the slowing of inflation.

Economic recovery will continue, although it will be limited due to the consequences of the war

Ukraine's economy is continuing to recover thanks to significant international support and the high adaptability of businesses and households to wartime conditions.

According to the NBU's estimates, Ukraine's real GDP grew by 3.4% in 2024, which was below the central bank forecast made in October. The pace of economic growth slowed compared to 2023. Apart from smaller harvests and weaker-than-expected external demand, the causes of this were the materialization of risks of more intensive hostilities, russia increasing its air attacks, and the resulting electricity shortages. The persistence of high security risks also restrained the return of migrants and led to significant labor shortages.

Taking into account security risks and the challenging situation in the labor market, the NBU has revised its real GDP growth projection for 2025 downward, to 3.6%. At the same time, the baseline scenario of the NBU's forecast continues to envisage that the economy will gradually return to normal functioning. Therefore, the pace of economic growth is expected to accelerate moderately in 2026–2027, to around 4%. On the one hand, the fallout from the war, which resulted in labor shortages and a production capital deficit, will continue to constrain the economy. On the other hand, investment being made into energy and production capacity, fiscal policy remaining rather loose, and private consumption rising on the back of an increase in household income will all contribute to recovery.

International support will be sufficient to finance the budget deficit without resorting to monetary financing, and to maintain the sustainability of the FX market

In 2024, Ukraine received USD 42 billion from its international partners in the form of loans and grants. These funds allowed the government to finance a substantial budget deficit (around 24% of GDP, excluding grants in revenues), and the NBU to maintain the sustainability of the FX market and to increase international reserves to a new all-time high (USD 43.8 billion at the end of 2024).

It is expected that in 2025 Ukraine will receive USD 38.4 billion in external financing. Taking into account the government's measures to increase its own revenues and borrowing on the domestic debt market, these funds should be enough to fully cover the planned budget deficit for this year (around 19% of GDP, excluding grants in revenues) without resorting to monetary financing. For its part, the NBU will be able to compensate for the structural FX deficit in the private sector and smooth out excessive exchange rate fluctuations. This will help maintain the sustainability of the FX market, in particular sustaining exchange rate dynamics that are consistent with achieving the 5% inflation target over the policy horizon.

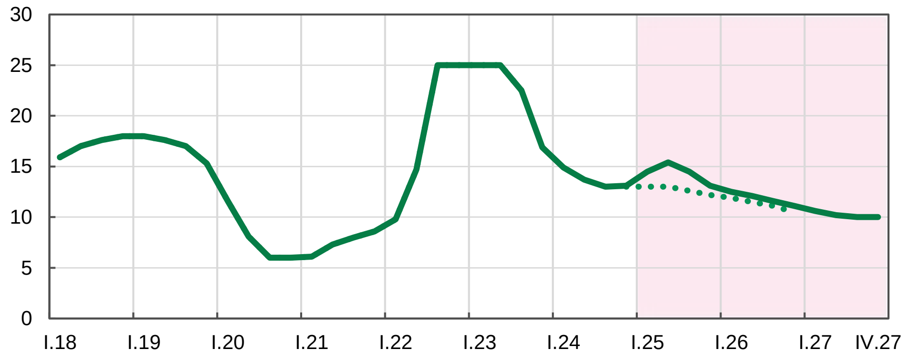
To maintain FX market sustainability, keep expectations under control, and to gradually bring inflation back to its 5% target over the policy horizon, the NBU raised the key policy rate to 14.5%

The acceleration of inflation in H2 2024 and the related deterioration in households' inflation expectations has decreased real yields on hryvnia savings instruments. The key policy rate hikes (by 0.5 pp in December and 1 pp in January) are intended to ensure that hryvnia savings are adequately protected from inflation, and to maintain public interest in hryvnia assets.

The NBU's updated macroeconomic forecast envisages further key policy rate hikes to curb inflation

The NBU is likely to continue tightening its interest rate policy at the Board's next monetary policy meetings if signs of persistent inflationary pressures and the threat of inflation expectations becoming unanchored are still present.

Figure 2. **Key policy rate, quarter average**



Source: NBU staff estimates.

The course of the full-scale war remains the key risk to inflation and economic development

russian aggression poses the risk of a further decline in economic potential, in particular due to the loss of people, territories, and production facilities. The speed of the economy's return to normal functioning conditions will depend on the nature and duration of the war.

The main risks caused by russian aggression remain the same:

- the emergence of additional budget needs, mainly those to maintain defense capabilities
- possible additional hike in taxes, which – depending on its parameters – might drive up pressures on prices
- further damage to infrastructure, especially energy infrastructure, which will restrain economic activity and put supply-side pressures on prices
- a deepening of adverse migration trends and a further increase of labor shortages in the domestic labor market.

There are also risks that international assistance will become less regular and that international economic trends will be less favorable than currently expected, in particular due to greater geopolitical polarization and the corresponding fragmentation of global trade.

However, positive scenarios could also materialize, primarily related to increased financial support from partners (in particular, by using the principal of immobilized russian assets to compensate for Ukraine's losses) and the international community's efforts to ensure a just and lasting peace for Ukraine. What is more, a further acceleration of European integration processes and the rebuilding of infrastructure, including energy infrastructure, are also possible.

Macroeconomic forecast (January 2025)

Indicators	2022	2023	2024		2025						2026						2027				
			actual/ estimate	forecast 10.2024	I	II	III	IV	current forecast	forecast 10.2024	I	II	III	IV	current forecast	forecast 10.2024	I	II	III	IV	current forecast
REAL ECONOMY, % yoy, unless otherwise stated																					
Nominal GDP, UAH bn	**5239**	**6628**	**7720**	7630	1839	1961	2359	2681	**8840**	8720	2073	2181	2602	2943	**9800**	9715	2276	2399	2866	3249	**10790**
Real GDP	**-28.8**	**5.5**	**3.4**	4.0	2.0	3.0	4.2	4.7	**3.6**	4.3	4.6	4.3	3.8	3.5	**4.0**	4.6	3.6	3.9	4.4	4.7	**4.2**
GDP Deflator	34.9	19.9	12.6	12.2	12.0	11.5	10.0	9.3	10.5	9.6	7.8	6.6	6.2	6.1	6.6	6.5	6.0	5.8	5.6	5.4	5.7
Consumer prices (period average)	20.2	12.9	6.5	6.1	-	-	-	-	12.4	9.5	-	-	-	-	6.2	5.7	-	-	-	-	5.0
Consumer prices (end of period)	**26.6**	**5.1**	**12.0**	9.7	14.3	13.6	12.0	8.4	**8.4**	6.9	7.2	5.6	5.4	5.0	**5.0**	5.0	4.9	4.9	5.0	5.0	**5.0**
Core inflation (end of period)	22.6	4.9	10.7	9.1	12.0	12.2	10.4	7.8	7.8	5.7	6.0	4.4	3.6	3.1	3.1	3.1	2.9	2.9	3.0	3.2	3.2
Non-core inflation (end of period)	30.6	5.7	13.8	10.4	17.2	15.4	14.0	9.2	9.2	8.2	8.5	7.0	7.4	7.3	7.3	7.3	7.3	7.1	7.2	7.1	7.1
raw foods (end of period)	41.6	2.2	13.2	6.7	16.7	18.1	15.4	6.8	6.8	5.9	7.8	5.5	4.2	3.0	3.0	2.8	3.2	3.7	3.6	3.1	3.1
administrative prices (end of period)	15.3	10.7	16.3	14.0	17.7	13.3	12.9	10.5	10.5	10.0	9.7	9.2	11.1	12.2	12.2	12.3	12.1	11.1	11.0	11.0	11.0
Nominal wages (period average)	6.0	17.4	22.0	21.0	22.8	18.8	14.3	12.1	16.7	16.0	11.5	11.4	10.0	9.5	10.6	8.9	8.2	7.7	8.3	8.2	8.1
Real wages (period average)	-11.4	3.7	14.4	14.0	8.2	3.7	1.3	2.6	3.8	6.5	3.6	5.0	4.2	4.0	4.2	2.9	3.1	2.6	3.1	3.0	3.0
Unemployment rate (ILO, period average)	21.1	18.2	13.1	14.2	-	-	-	-	10.8	11.6	-	-	-	-	10.5	10.6	-	-	-	-	11.0
FISCAL SECTOR																					
Consolidated budget balance, UAH bn*	**-845**	**-1332**	**-1351**	-1347	**-**	**-**	**-**	**-**	**-332**	-1640	**-**	**-**	**-**	**-**	**-1104**	-1182	**-**	**-**	**-**	**-**	**-641**
% of GDP*	-16.1	-20.1	-17.5	-17.7	-	-	-	-	-3.8	-18.8	-	-	-	-	-11.3	-12.2	-	-	-	-	-5.9
excluding grants from revenues, % of GDP	-25.3	-26.6	-23.7	-23.3	-	-	-	-	-19.3	-19.6	-	-	-	-	-11.9	-12.4	-	-	-	-	-7.0
BALANCE OF PAYMENTS (analytical presentation)																					
Current account balance, USD bn	8.0	-9.6	-14.6	-16.3	-1.9	0.3	-0.8	5.1	2.6	-27.9	-6.7	-7.0	-7.7	-6.9	-28.3	-28.4	-7.4	-6.4	-7.7	-6.3	-27.9
Exports of goods and services, USD bn	57.5	51.3	56.1	57.2	14.0	13.0	13.9	17.2	58.1	57.7	15.3	14.7	16.0	17.5	63.5	63.6	15.9	15.7	16.5	18.9	67.0
Imports of goods and services, USD bn	83.3	89.2	91.8	92.1	23.7	23.1	24.7	25.4	96.9	95.6	24.0	23.9	25.5	25.9	99.3	97.3	24.6	24.3	26.1	27.1	102.2
Remittances in Ukraine, USD bn	12.5	11.3	9.6	9.9	2.5	2.4	2.5	2.7	10.1	11.1	2.7	2.8	2.9	3.0	11.4	12.4	2.9	2.9	3.0	3.1	12.0
Financial account, USD bn	11.1	-18.9	-14.3	-15.2	2.6	1.6	1.1	1.1	6.4	-24.9	-7.0	-8.4	-6.0	-5.0	-26.3	-22.2	-6.5	-7.8	-7.1	-8.4	-29.7
BOP overall balance, USD bn	**-2.9**	**9.5**	**0.0**	-0.8	-4.5	-1.3	-1.9	3.9	**-3.8**	-2.9	0.2	1.4	-1.7	-1.9	**-2.0**	-6.2	-0.9	1.3	-0.6	2.0	**1.9**
Gross reserves, USD bn	**28.5**	**40.5**	**43.8**	43.6	39.3	38.3	36.5	40.5	**40.5**	41.0	41.2	42.1	40.9	38.5	**38.5**	34.7	38.3	39.4	38.4	40.2	**40.2**
Months of future imports	3.8	5.3	5.4	5.5	4.9	4.7	4.4	4.9	4.9	5.1	4.9	5.0	4.9	4.5	4.5	4.1	4.4	4.5	4.4	4.5	4.5
MONETARY ACCOUNTS (cumulative since the beginning of the year)																					
Monetary base, %	**19.6**	**23.3**	**7.7**	13.3	2.9	4.9	7.4	11.9	**11.9**	13.1	2.0	4.8	6.8	13.4	**13.4**	11.4	0.4	3.6	5.9	10.5	**10.5**
Broad money, %	**20.8**	**23.0**	**13.4**	13.3	0.7	3.5	4.9	10.3	**10.3**	11.2	1.1	3.5	5.5	9.6	**9.6**	9.7	2.1	5.3	6.3	9.1	**9.1**
Velocity of broad money (end of year)	**2.1**	**2.2**	**2.2**	2.2	-	-	-	-	**2.3**	2.2	-	-	-	-	**2.3**	2.3	-	-	-	-	**2.3**

* The financing under the ERA program has been reclassified as grants and included in revenues

Comments on the dynamics of the main indicators in the macro forecast and factors behind their revision

Indicators	2024	2025	2026	2027	Factors behind the revision
Inflation, %, eop	**12.0**	**8.4**	**5.0**	**5.0**	Rising food prices driven by adverse weather conditions, the pass-through of higher production costs, including those resulting from labor market mismatches
	2.3	1.5	0.0		
Real GDP growth, %	**3.4**	**3.6**	**4.0**	**4.2**	Revised potential GDP due to further losses in production factors and the ongoing impact of shelling
	-0.6	-0.7	-0.6		
Nominal GDP, UAH bn	**7720**	**8840**	**9800**	**10790**	Revised data for 2023, higher GDP deflator but lower real growth
	90	120	85		
Consolidated budget balance (excluding grants and ERA financing from revenues), % of GDP	**-23.7**	**-19.3**	**-11.9**	**-7.0**	Higher budget expenditures financed by increased foreign aid at the end of 2024, higher nominal GDP
	-0.4	0.3	0.5		
Current account balance, USD bn	**-14.6**	**2.6**	**-28.3**	**-27.9**	Financing under the ERA program expected mostly in 2025 reclassified as grants
	1.7	30.5	0.1		
Gross international reserves, USD bn	**43.8**	**40.5**	**38.5**	**40.2**	Higher inflows of debt capital into the private sector in 2026
	0.2	-0.5	3.8		
Key policy rate (period average), %	**13.7**	**14.4**	**11.8**	**10.2**	Higher inflationary pressures
	0.1	1.7	0.6		

The indicator has been revised downwards (pp)

The indicator has been revised upwards (pp)

Forecast assumptions

Indicators		2022*	2023*	2024	2025	2026	2027
Official financing	USD bn	32.2	42.9	41.9	38.4	25.0	15.0
Migration (net, excluding russia and belarus)	m		-0.2	-0.5	-0.2	0.2	0.5
Real GDP of Ukraine's MTP (UAwGDP)	% yoy	3.6	1.5	1.9	2.5	2.6	2.7
Consumer inflation in Ukraine's MTP (UAwCPI)	% yoy	13.8	7.6	5.1	3.4	2.7	2.5
World prices:**							
Steel price, Steel Billet Exp FOB Ukraine	USD/t	618.1	539.7	504.1	490.0	501.5	508.0
	% yoy	0.5	-12.7	-6.6	-2.8	2.3	1.3
Iron ore price, China import Iron Ore Fines 62% FE	USD/t	121.4	120.6	109.4	92.6	81.2	76.2
	% yoy	-24.9	-0.7	-9.3	-15.3	-12.3	-6.2
Steel price, No.1 Hard Red Winter, ordinary protein, Kansas City	USD/t	360.2	272.3	201.5	218.7	232.2	237.3
	% yoy	35.5	-24.4	-26.0	8.5	6.2	2.2
Corn price, Yellow #2 Delivery USA Gulf	USD/t	318.4	252.7	190.6	213.8	223.3	229.5
	% yoy	22.7	-20.6	-24.6	12.2	4.4	2.8
Oil price, Brent	USD/bbl	99.8	82.6	80.7	74.7	73.1	73.1
	% yoy	41.8	-17.2	-2.3	-7.4	-2.1	0.0
Natural gas price, Netherlands TTF	USD/kcm	1355.9	465.6	393.9	404.7	384.7	336.5
	% yoy	135.9	-65.7	-15.4	2.7	-4.9	-12.5
Volumes of gas transit	bcm	20.6	14.6	15.0	0.0	0.0	0.0
Harvest of grain and leguminous crops	t m	53.9	59.8	55.2	60.1	62.3	64.9
Minimum wage**	UAH	6550	6700	7775	8000	8370	8950

** Actual data*

*** Annual average.*