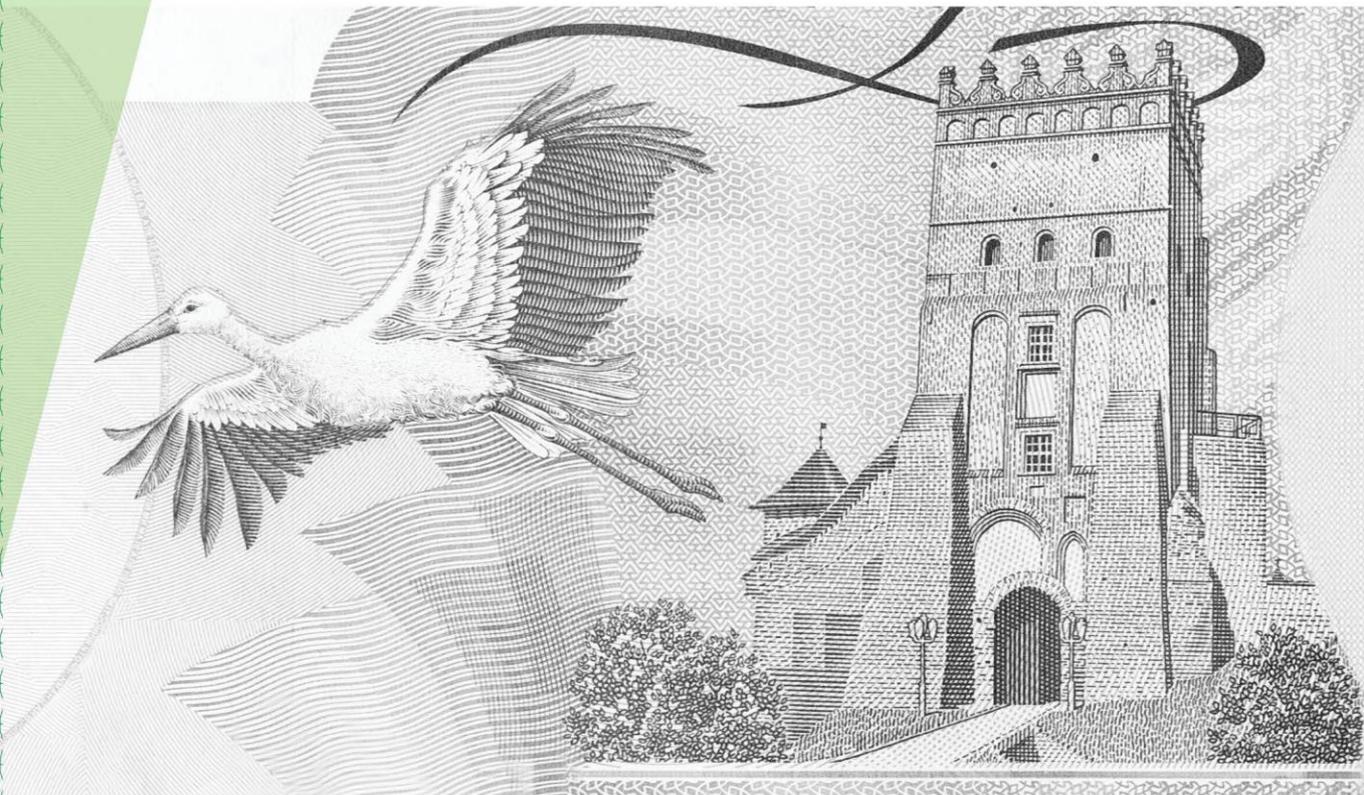




National Bank  
of Ukraine

# Macroeconomic and Monetary Review

October 2020



# Summary

## External Environment

Throughout most of October, Ukrainian exporters continued to see an improvement in global commodity market conditions, with demand and supply factors both playing a role. Steel prices rose as global demand recovered amid large-scale government support by many countries. Grain prices increased due to growing negative expectations about the harvests of these crops. Oil prices fluctuated around USD 42 per barrel, driven by two counterbalancing factors: the effects of the OPEC+ agreement and the weakening of demand as the coronavirus pandemic took a turn for the worse. Natural gas prices rose on the back of an increase in demand after the heating season started in the Northern Hemisphere. Foreign investors took greater interest in risky assets, including those of EMs, thanks to expectations of further fiscal stimulus in the United States and the IMF's improved outlook on the global economy. Tighter quarantine measures in several European countries, primarily in Germany and France, worsened expectations regarding economic recovery later this month. As a consequence, oil prices plummeted, while EM currencies lost ground against the U.S. dollar, offsetting the strengthening since the beginning of October.

## Inflation

Consumer inflation in September 2020 slowed to 2.3% yoy (down from 2.5% yoy in August) and was below the 5% ± 1 pp target range, as expected. The decline in inflation was mainly due to the slowdown in food price growth. The latter was in part due to temporary supply factors amid the low-quality of vegetables from the new harvest, an expanded supply of imported products and lower production costs. Core inflation also decelerated slightly (to 3.1% yoy from 3.2% yoy in August), primarily driven by food prices. In addition, services prices grew somewhat more slowly, likely due to weaker demand for some services (such as those provided by cafes, fast-food restaurants, sports facilities, etc.) amid an increase in morbidity. Excluding food prices, consumer inflation accelerated, driven by higher natural gas tariffs, a weakening of the hryvnia, and a recovery in economic activity.

The fall in producer prices continued to slow in September 2020 (to 1.7% yoy from 4.7% yoy in August). This was mainly attributable to stronger external demand and higher global prices for Ukraine's main exports (ore, metals, sunflower oil), a weakening of the hryvnia in August–September, and higher energy prices.

## Economic Activity

In September, the fall in the IKSO deepened (to 6.8% yoy from 1.6% yoy in August), primarily due to a significant decline in agriculture. The latter was driven by poorer corn and oilseeds yields and the delayed start of the harvesting of these crops. The slump in agriculture had a negative impact on freight turnover, while tighter quarantine restrictions weighed down passenger turnover. At the same time, consumer and investment demand continued to show signs of recovery, as evidenced by robust trade growth (amid rising household incomes and improving consumer sentiment) and construction (in part due to higher budget expenditures on infrastructure development). The decline in industry slowed as domestic and external demand has been recovering.

## Labor Market

In September, wage growth accelerated (to 12.3% yoy in nominal terms and 9.7% yoy in real terms) due to an increase in the minimum wage, the lifting of caps on public sector wages, and wage supplements for healthcare workers. Labor demand in September 2020 remained robust. Interest in finding work both in Ukraine and abroad also grew.

## Fiscal Sector

In September 2020, the state budget ran a significant deficit of UAH 40.5 billion. Budget expenditures were significantly increased (by 29.0% yoy) not only in priority areas, but also in other areas, including defense, public order, education, etc. At the same time, budget revenues grew (by 12% yoy) due to tax revenues, which have been rising for two consecutive months. This was due to the revival of trade, the growth in nominal wages, the weakening of the hryvnia, and better [administration](#) of certain taxes. Local budgets also recorded a deficit in September (UAH 3.3 billion). As a result, the consolidated budget ran a significant deficit.

### Balance of Payments

The current account recorded a deficit of USD 0.2 billion in September due to scheduled repayments on restructured domestic government debt securities and a widening of the merchandise trade deficit. Specifically, against a backdrop of further recovery in domestic demand, the decline in imports of consumer and investment goods decelerated, and this was only partially offset by a reduction in energy purchases. Exports of goods reached last year's level due to increased supplies of metal and mining products, but growth in exports was restrained by the current year's lower harvest. The surplus in the trade in services remained significant despite an uptick in foreign tourism.

Financial account outflows reached a significant USD 1.8 billion, driven by a peak in repayments of external debt by the government. Coupled with the current account deficit, this led to a decrease in gross international reserves to USD 26.5 billion. However, international reserves remained higher than at the beginning of the year, and were sufficient to cover 4.5 months of future imports.

### Monetary Conditions and Financial Markets

In October, [the NBU Board decided](#) to keep its key policy rate unchanged, at 6% per annum. However, monetary policy remains accommodative, which will support economic recovery and help return inflation to the target range.

Throughout October, the [UONIA](#), the indicator of interest rates in the interbank lending market, hovered in a narrow range just above the lower bound of the NBU's interest rate corridor. As demand weakened, the yields on hryvnia domestic government debt securities increased in the primary and secondary markets. In September, the banks continued to reduce hryvnia rates for their customers.

In October, supply and demand in the FX market were almost in balance. As a result, the value of the hryvnia did not change significantly against the dollar over the month, although on average the hryvnia was weaker than in September..

*The Macroeconomic and Monetary Review is a translation of the original report in Ukrainian. If there are any discrepancies between the original document and its English translation, readers should consider the Ukrainian version of the report as correct.*