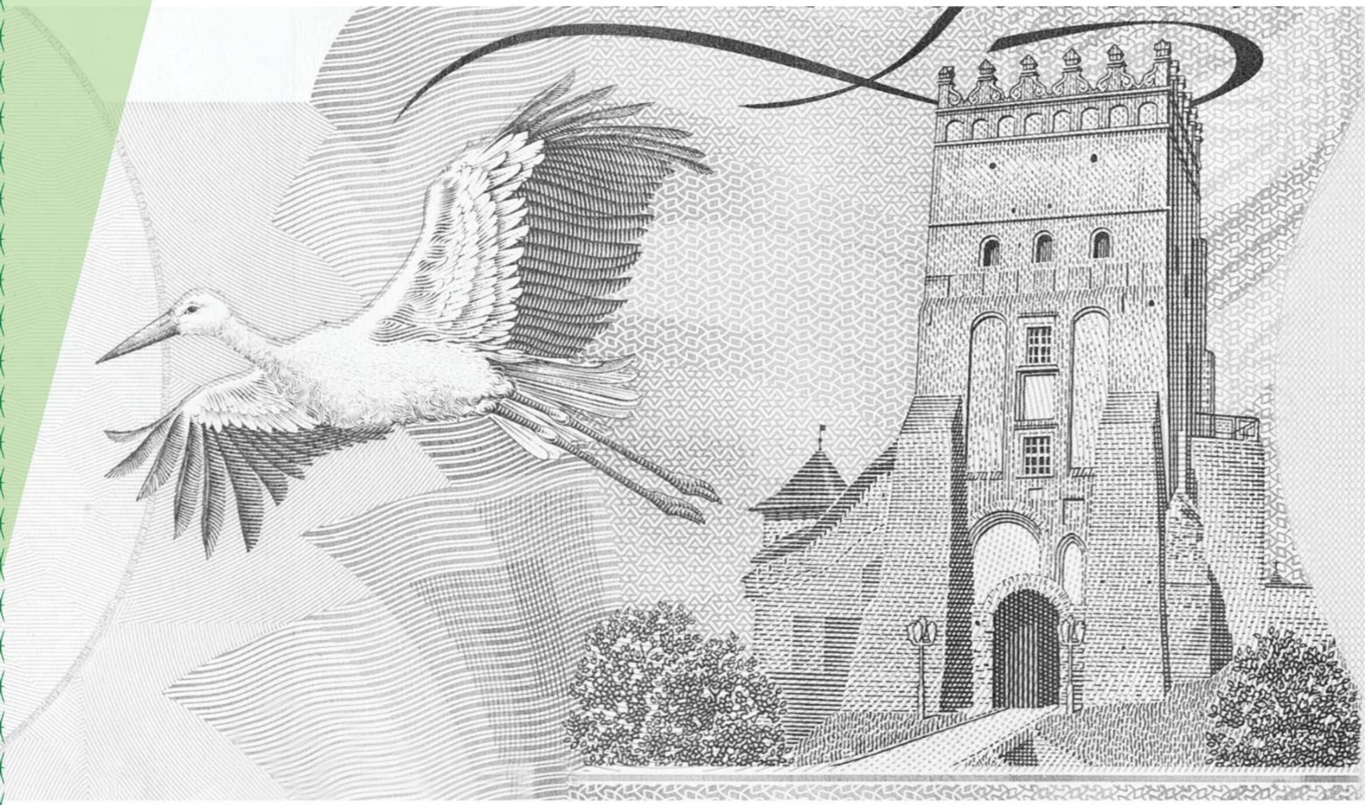
National Bank of Ukraine

Macroeconomic and Monetary Review

September 2018



SUMMARY

● In September 2018, the Ukrainian exporters faced worsened global price environment due to lower steel prices in selected regional markets, as well as prices for grains and sunflower oil. Meanwhile, oil prices rallied as supply tightened. In global financial markets, investors adopted a wait and see mode towards emerging market assets. On one hand, escalation of trade wars weighed on investors' sentiments. On the other hand, favorable macroeconomic data sustained their interest.

● The Ukrainian foreign exchange market calmed in September as FX demand fever subsided. Moreover, in the cash market, households turned back to net sellers of FX. In addition, the National Bank of Ukraine maintained its presence in the market with the aim of reducing FX volatility. Meanwhile, the NBU's role declined compared with August, and interventions were conducted both on the sale and the purchase sides.

● Consumer prices slightly accelerated, to 9.0% yoy in August, despite the easing pressure from food prices, as the supplies of both domestic and imported products expanded. In addition, price growth for non-foods remained contained given favorable FX market developments during the first half of the year. However, the underlying inflation pressures remained elevated amid steady consumer demand – core inflation decelerated slightly, to 8.7% yoy. In addition, a faster increase in fuel prices and an acceleration in wage growth (to 26.2% yoy and 15.7% yoy in nominal and real terms) spurred administered price inflation.

● In view of sustained high underlying inflation pressure and upside risks to bringing inflation back to the medium-term target, including due to external environment risks, the NBU Board decided to raise the key policy rate by 50 bps to18.0% per annum effective from 07 September 2018. The interest rates on interbank loans and yields on the hryvnia government bonds responded to the key policy rate hike. The hryvnia retail bank interest rates rose slightly in August, reflecting the previous policy rate hikes and narrowed liquidity in the banking system.

● The IKSO growth slowed down in January – August 2018, to 3.0 yoy. The repair works at some plants caused weakness in the production growth of the metallurgy industry and were among reasons for lower electricity production (mainly, by combined heat and power plants). A more challenging freight transportation through the Sea of Azov for Ukraine were another reason behind worsened performance of the industry and some other sectors (wholesale trade and cargo turnover). Instead, the faster harvesting campaign this year and higher yields of late crops drove the agricultural production index higher. Retail trade and passenger turnover, as well as non-energy imports (more specifically, automobiles, clothes and footwear, some consumer goods, etc.) continued to grow at solid paces. This signaled steady consumer demand, driven by robust real wage growth.

● Improved crop production supported export growth in August, which, however, slowed compared to July, due to lower volumes of ferrous metal exports. At the same time, import growth slowed as well due to a significant reduction in volumes of imported coal and petroleum products. As a slowdown in imports outpaced exports, the current account deficit narrowed compared to July, to USD 0.6 billion. Mainly owing to the discount eurobonds placed by the government, net financial account inflows amounted to USD 0.6 billion, fully offsetting the current account deficit. However, international reserves declined to USD 17.2 billion as of the end of August, or 2.9 months of future imports, due to repayments to the IMF.

● In August, the state budget recorded a significant surplus of UAH 25.2 billion, primarily due to a sharp slowdown in expenditure growth. The latter was largely due to a decrease in current transfers, which include targeted funds allocated to the local budgets for the payment of social benefits and subsidies (due to a moderate rise in utility tariffs this year, strong growth in wages and pensions, as well as amendments to the procedures for granting subsidies, the number of households – grantees has decreased substantially). Revenue growth was supported by a further rise in tax receipts from imported goods amid the weakening of the hryvnia in August, robust wage growth, and increased profits of profitable enterprises. With local budgets adding to a positive balance, the consolidated budget showed a significant surplus of nearly UAH 27 billion.

The Macroeconomic and Monetary Review is a translation of the original Report in Ukrainian. In case of any discrepancies between the original document and its English translation, readers should consider the Ukrainian version of the Report as correct.