NATIONAL
BANK OF
UKRAINE

Macroeconomic and Monetary Review

November 2017

Monetary Policy and Economic Analysis Department

Summary

● In November 2017, global prices for commodities prevailing in Ukrainian exports moved in different directions. Steel prices were declining, while grain prices were gradually rising. Global steel prices decreased, except for the Chinese market, as demand weakened, primarily in the construction sector, amid higher supply. Wheat prices were rising, while corn prices were almost steady. Oil prices were predominantly rising on lower US oil inventories and the expected extension of the OPEC+ agreement. Emerging markets contined to enjoy favorable global market conditions.

● In October 2017, consumer price inflation expectedly decelerated to 14.6% yoy as raw food prices and administered prices and tariffs rose at a slower rate. In monthly terms, the consumer price index rose 1.2%. Actual inflation came in close the forecast published in the October 2017 Inflation Report. Core inflation in October stood at 8.1% yoy. The growth in producer price index continued to decelerate (down to 18.8% yoy).

● The Index of Key Sectors Output resumed declined in October by 1.6% yoy; however, it continued to increase on a cumulative basis (by 2.0% yoy for the first ten months of 2017). October's decline was largely driven by a deeper decrease in agricultural output (down by 9% yoy), primarily due to lower corn and sunflower harvests. Industrial output rose 0.4% yoy with the major contribution coming from food manufacture, chemical production and manufacture of fabricated metal products. Construction growth accelerated on the back of high capital budget expenditures and favorable weather conditions. The growth in wholesale trade also picked up, supported by strong exports of vegetable oils and fats and higher imports, particularly coal and fertilizers. Meanwhile, retail trade growth slowed down.

● In recent months labor demand has weakened. Meanwhile, the average nominal wages continued to grow at a fast pace (37.9% yoy in October). Along with deceleration in inflation, this resulted in the acceleration in real wage growth (to 19.9% yoy).

● In October, the state budget recorded a deficit (UAH 13.6 billion), although it narrowed compared with the previous month. In particular, the launch of the pension reform and the increase in domestic debt payments led to a spar acceleration in expenditure growth, while revenue growth slowed down. At the same time, local budgets returned to a surplus due to an increase in their own revenues. As a result, the consolidated budget showed a moderate deficit in October (UAH 10.4 billion) and a still hefty cumulative surplus (UAH 31.2 billion for January – October 2017).

● The current account deficit narrowed compare to the previous month (to USD 0.4 billion) owing to the primary income account returning to surplus and an ongoing rise in remittances. However, the merchandise trade deficit widened due to lower grain supplies and a continued rise in energy and machinery imports. Net financial account inflows stood at USD 0.6 billion. Unlike previous months, net private sector inflows were backed by the banking sector, while corporates mainly repaid their external liabilities. Owing to the overall BoP surplus (USD 0.2 billion), international reserved grew to USD 18.7 billion as of the end of October, or 3.7 months of future imports.

● At its last monetary policy meeting the NBU Board decided to hike the key policy rate by 1 pp to 13.5% pa, effective from 27 October 2017. The decision to tighten monetary policy was mainly prompted by the need to prevent further deterioration of inflation expectations. The tighter monetary policy will help reduce consumer inflation and bring it closer to the target in Q3 2018. Market interest rates for hryvnia resources, parimarily interbank interest rates and government bond yields, responded swiftly to the rise in key policy rate. In the meantime, banks' hryvnia deposit and loan portfolios kept growing.

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