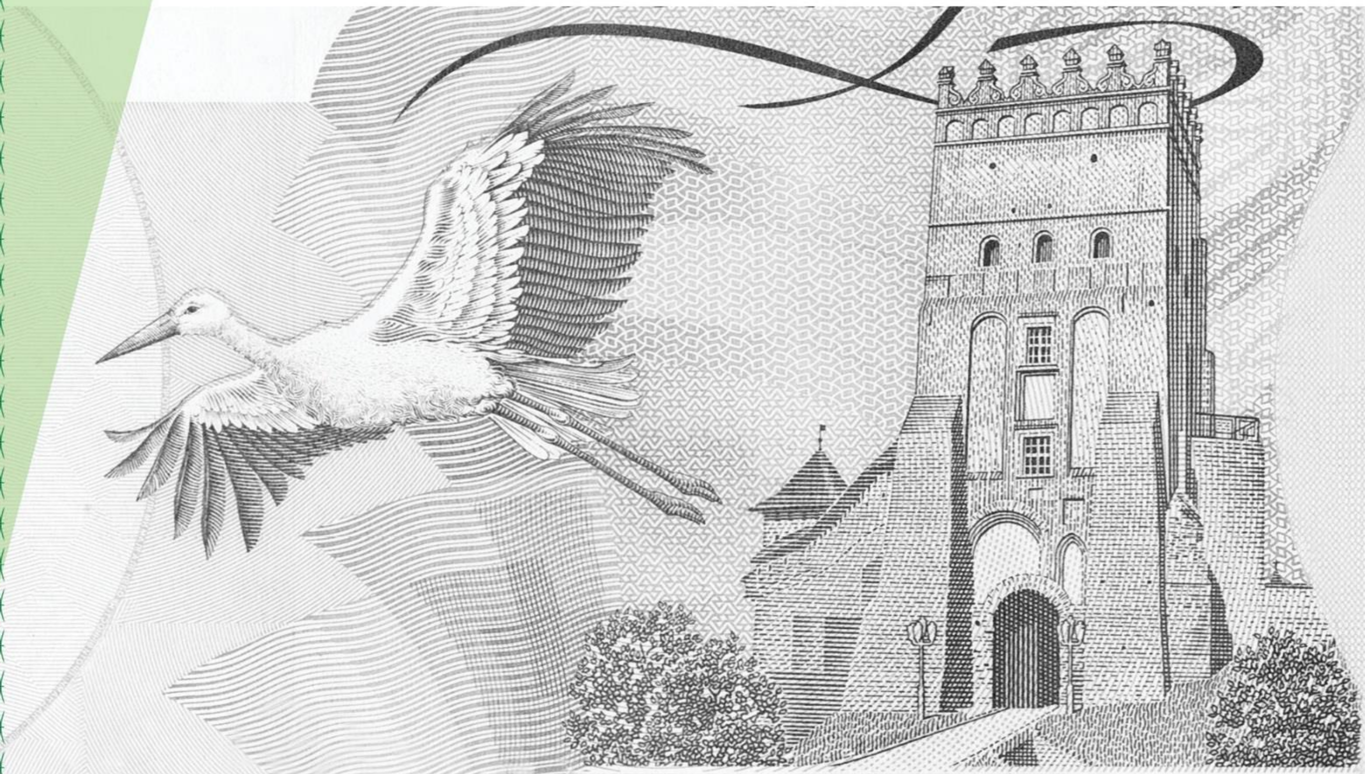
National Bank
of Ukraine

Macroeconomic and Monetary Review

December 2018



Summary

● In December, the Ukrainian exporters faced a worsening price environment, mainly due to a further decrease in steel prices. At the same time, grain prices have edged up due to lower yields. Oil prices continued to plunge in response to the supply glut, retreating to their lowest since September 2017. In global financial markets, investor appetite to risky assets, including emerging market assets, weakened on the back of worsened global growth outlook.

● In November 2018, consumer price inflation accelerated to 10.0% yoy. This can be largely attributed to an increase in the prices of natural gas for households in November (by 22.9%). Moreover, core inflation accelerated to 8.9% yoy, reflecting increased costs, including labor costs, and the sustained domestic demand. At the same time, these factors were partially offset by a slow pace of growth in the raw food prices and a deceleration in fuel price growth. Consumer price inflation was generally in line with the NBU's forecast published in its October 2018 Inflation Report.

● In January - November, the growth in the IKSO index slowed, to 4.1% yoy, primarily due to a decrease in crop production index. The latter can be attributed to a faster pace of crop harvesting in the previous periods and more complicated weather conditions in November this year compared to November a year before. The weather conditions also weighed on construction, but contributed to an improved performance of the energy industry. The ongoing repair works in metallurgical plants and difficulties with the transportation of raw materials and finished goods, including via ports in the Sea of Azov, deepened the decline in metallurgy in November. As a consequence, the performance in the production-related sectors, such as coke production, coal and metal ore mining, as well as cargo turnover, worsened. The decline in the food and chemical industries and machine building deepened as well. As a result, cumulatively, the overall industrial output growth slowed, to 1.6% yoy in January - November. Instead, robust growth in retail sales and passenger turnover pointed to sustained consumer demand.

● In November, the state budget recorded a surplus of UAH 6 billion. Revenue growth accelerated (to 24.5% yoy), mainly due to domestic tax receipts and a portion of dividend payments (UAH 8.1 billion) that come out of the Naftogaz PJSC's profit for 2017. At the same time, expenditures returned to growth (by 22.6% yoy), mostly due to higher domestic debt service spending than last year. Local budgets in November also reported a UAH 1.6 billion surplus, primarily owing to improved revenues. As a result, the consolidated budget showed a positive balance in November, bringing a tally surplus to UAH 22 billion for January-November.

● In November, the current account deficit narrowed to USD 0.3 billion, bringing the cumulative deficit for 11 months of the year to USD 4.4 billion, notably wider than a USD 1.7 billion deficit in January – November 2017. Worsening performance in metallurgical production continued to weigh on export growth, however, food exports hit a new record. Import growth slowed considerably on both smaller amounts of coal purchases and some softening of strong consumer demand for imported goods in previous months amid favorable FX market performance. Financial account inflows rose to USD 1.6 billion owing to the receipt of funds from sovereign Eurobonds issued in October. For January – November, financial account inflows totaled USD 5.5 billion. The overall balance of payments recorded a surplus, that enabled the accumulation of international reserves, up to USD 17.7 billion as of the end of November.

● The FX markets remained calm during December owing to the increased FX supply from the bank clients, as well as improved market sentiment amid the new IMF program approval and the disbursement of official financing from other international organizations. As a result, the net FX purchases of the NBU amounted to USD 339 million. Along with the disbursement of official financing, this led to an increase in international reserves to USD 20.7 billion as of 27 December 2018, or 3.5 months' of future imports.

● At its last monetary policy meeting, the NBU Board decided to hold the key policy rate unchanged, at 18% per annum. According to the NBU, current and forecast monetary conditions are sufficiently tight to bring inflation to its medium-term target of 5% in 2020. Furthermore, in order to be more flexible in responding to changes in liquidity stance of the banking system of Ukraine, the NBU has introduced changes to the operational framework of its monetary policy effective 11 January 2019.

● Hryvnia market rates continued responding to past policy rate hikes and the government operations. The increase in hryvnia retail bank interest rates in November was also affected by market-specific factors.

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.