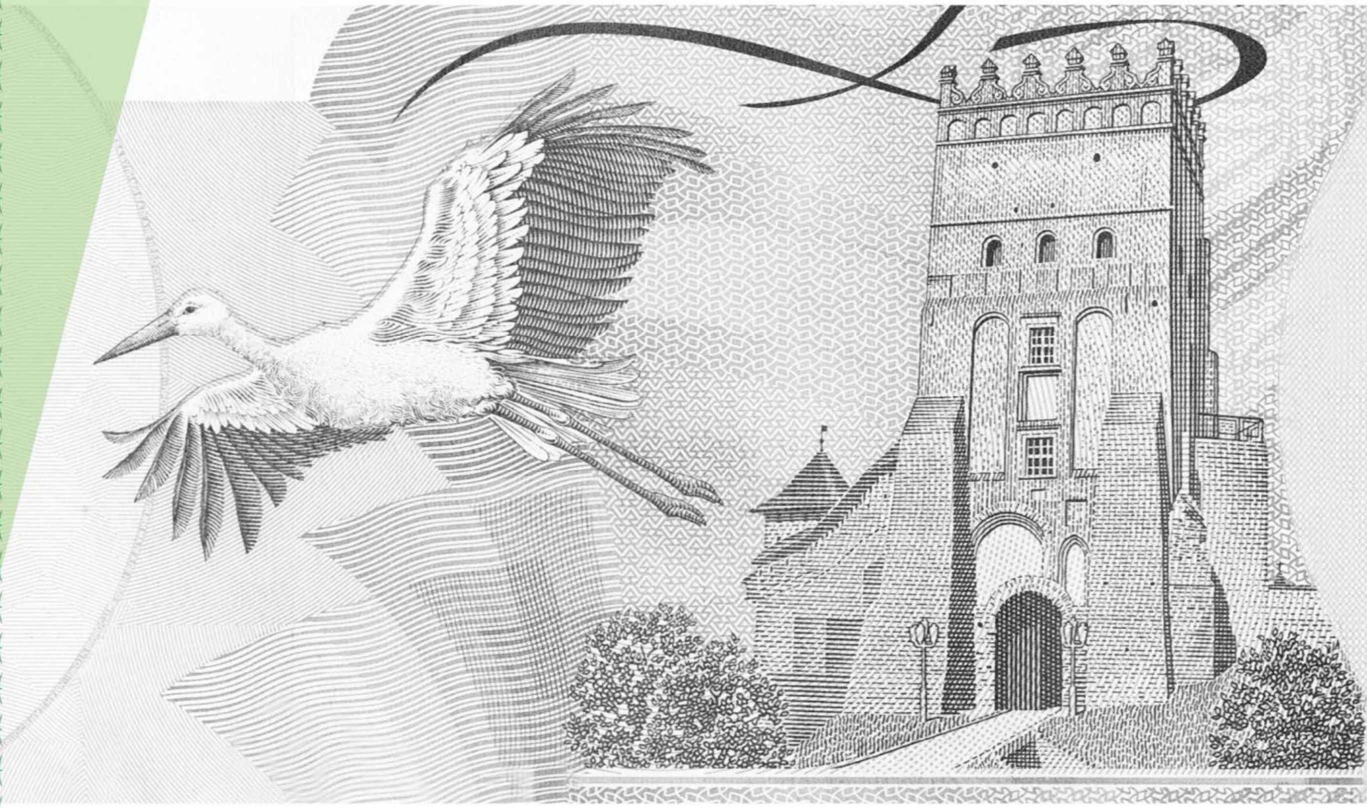
National Bank of Ukraine

Macroeconomic and Monetary Review

August 2019



Summary

In August, global commodity prices, in particular those for steel, fuels, grains, mostly declined. Emerging markets also faced worsening global financial conditions as investor risk appetite fell, triggering demand for the sovereign bonds of advanced countries and a depreciation of the majority of emerging market currencies. Both the commodity and financial markets were dominated by heightened concerns regarding a global economic slowdown amid intensifying geopolitical conflicts and trade tensions.

In July, consumer inflation accelerated somewhat (to 9.1% yoy) due to price pressure from raw foods. At the same time, core inflation remained unchanged at the previous month's level of 7.4% yoy. Tight monetary policy continued to be a significant factor in containing underlying inflationary pressures, in particular due to further strengthening of the hryvnia. In addition, declining oil and natural gas prices contributed to a year-on-year decrease in fuel prices. The same factor held back producer price inflation, which nevertheless accelerated to 6.7% yoy, driven by electricity prices, which rose after pricing approaches were changed.

In July, the IKSO grew more rapidly (by 5.9% yoy), mainly due to the contribution of agriculture, thanks to high crop yields and faster rates of harvesting early grains. Growth in construction also accelerated significantly, in part due to higher capital expenditures from the state budget and improved performance of housing construction. The growth in retail trade turnover continued to be strong, driven by sustained growth in household income (nominal and real wage growth accelerated in July to 19.6% yoy and 9.5% yoy, respectively) and robust consumer sentiment. Industrial production performance improved on account of metallurgy, the food industry, and machinery. Overall, however, the industrial production index was lower than a year ago, primarily due to the energy sector, which was affected by colder weather.

In July, the state budget recorded a minor deficit (UAH 2 billion). The deficit was lower compared to both the previous month and the same month a year ago. This can be attributed to a significant increase in revenues, largely due to the transfer of a part of profits for 2018 by Naftogaz NJSC to the state budget, despite the accelerating expenditures. In addition, tax performance improved, driven by robust wage growth, increased imports, and slightly lower VAT refunds. In July, local budgets moved back into surplus (UAH 3.7 billion), bringing the consolidated budget into surplus (UAH 1.7 billion) as well.

Merchandise exports increased rapidly in July, due to the shipments of newly harvested grains. Import growth accelerated as well, driven by purchases of vehicles and alternative energy equipment. As a result, the goods trade deficit widened, leading to an increase in the current account deficit (to USD 0.6 billion). The financial account recorded significant inflows (USD 1.9 billion) for the second month running. Unlike in previous months, however, the financial account inflows were driven not only by the public sector, but also by the placing of Eurobonds by private companies. Thanks to a significant surplus in the overall balance of payments (USD 1.3 billion), international reserves had risen to USD 21.8 billion, or 3.4 months of future imports, by the end of July.

The weighted average yield on government securities fell in August, driven down by the continuation of the monetary policy easing cycle (the NBU cut the key policy rate by 50 bp in July, to 17.0%), the likelihood of a further decrease in the key policy rate in line with the NBU's published interest rate forecast, and a decrease in the supply of domestic government bonds. The UIIR fluctuated in a narrow range during the greater part of the month, staying close to the lower bound of the NBU's interest rate band. Its rise in late August was transitory, driven by the narrowing of liquidity that is typical for periods of quarterly tax payments to the budget. Market-specific factors also largely affected the cost of bank retail loans and deposits.

In the FX market, the hryvnia strengthened for most of August, primarily due to a significant supply of foreign currency by exporters. This allowed the NBU to continue to replenish international reserves without countervailing market trends.

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.