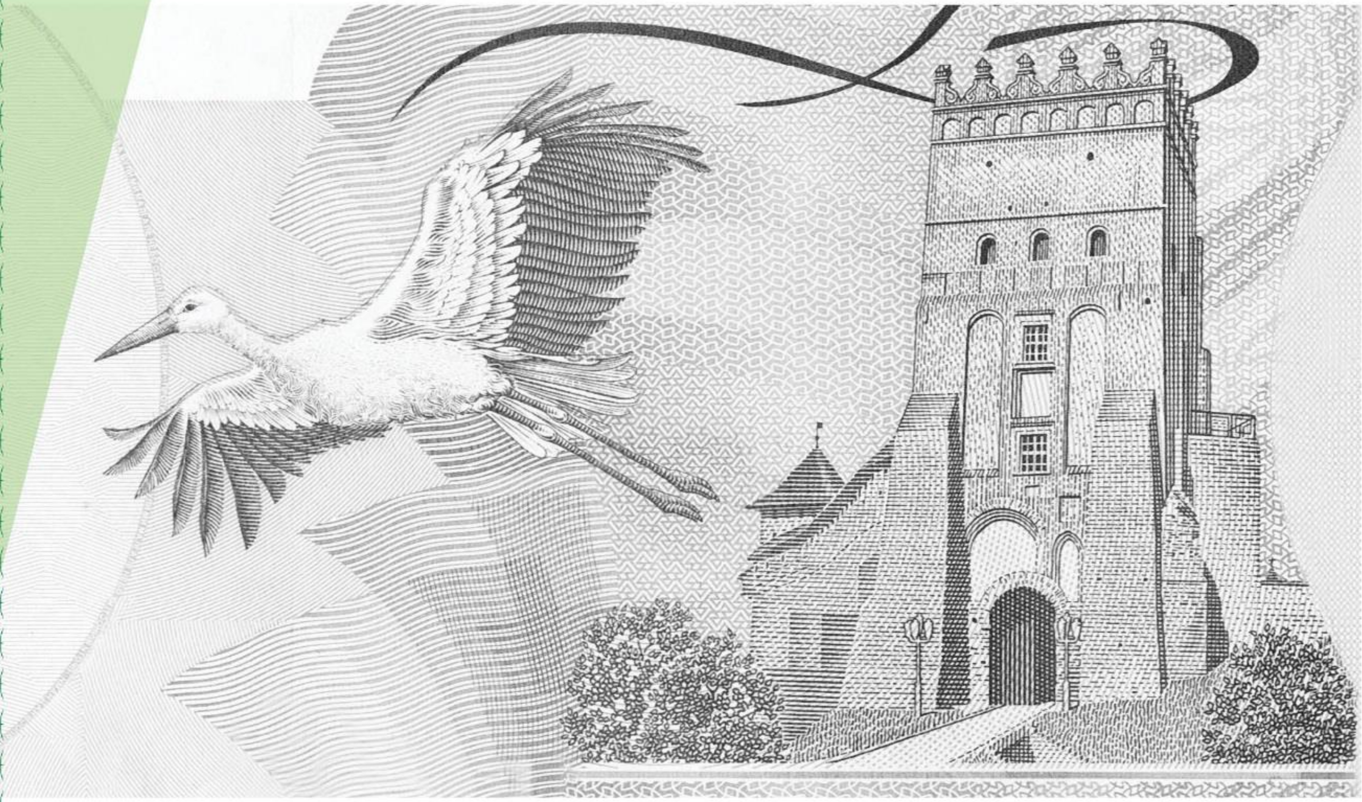
National Bank of Ukraine

Macroeconomic and Monetary Review

May 2019



SUMMARY

May 2019 was marked by the escalating trade conflict between the United States and China, which had a significant effect on the global commodity and financial markets. Thus, despite upward pressure from declining supplies, oil prices ended the month lower due to concerns over global growth. The latter factor also contributed to sluggish steel demand, driving steel prices lower. Meanwhile, grain and iron ore prices rose, reflecting unfavorable weather conditions in the United States, and disruptions to supplies from Brazil and Australia. The shift in trade tensions between the United States and China into a higher gear was one of the main factors triggering capital flight to safe-haven assets and the selloff of emerging market (EM) assets. As a result, most EM currencies depreciated against the U.S. dollar.

In April 2019, annual consumer price inflation accelerated somewhat (to 8.8% yoy). This was due to the combined effect of temporary factors, including disruptions to the supply of oil products from Belarus and the restrictions on exports of energy products to Ukraine announced by Russia, which pushed fuel prices higher. Another temporary factor was the emergence of speculative demand for some raw food products amid their scarce supply, which, in turn, caused their prices to accelerate. In contrast, core inflation continued to decline, in part due to the NBU's tight monetary policy. Annual producer price inflation was the lowest in five years thanks to a decline in natural gas and electricity prices.

Between January and April 2019 the performance indicators in key sectors, excluding agriculture, improved, with the Index of Key Sectors Output (the IKSO) up by 1.4% yoy. In particular, the growth of retail turnover and passenger transportation accelerated, supported by steady consumer demand against the backdrop of robust wage growth (by 20.8% yoy in nominal and by 11.0% yoy in real terms in January – April). Also, industry returned to cumulative growth, in particular due to a faster growth in metallurgy. High construction rates and improved performance in the engineering sector signaled about a ramp-up in investment.

In April, the state budget ran a significant surplus (UAH 24.4 billion), primarily driven by the transfers of distributable profit from the NBU. These transfers boosted the revenue side of the state budget by 41.2% yoy. At the same time, the growth in tax receipts remained modest, mainly due to the effects of the ruling made by the Stockholm Arbitration Court last year. State budget expenditures returned to growth, fueled by expenditures to support the Pension Fund of Ukraine and public debt servicing. In April, local budgets also recorded a surplus. As a result, the consolidated budget ran a surplus of UAH 26.6 billion.

In April, the current account balance was close to zero, with the deficit being only USD 8 million. Nevertheless, this month's outcome was worse than last April because of a widening in the deficit in the trade in goods, which was driven by an increase in energy imports and slower export growth. In the financial account, strong demand from non-residents for hryvnia-denominated securities brought about net capital inflows to the public sector. This almost offset the net outflows from the private sector, which mainly resulted from the banking sector's redemption of Eurobonds. The overall balance of payments was close to zero, leaving gross international reserves almost unchanged in late April compared to March, at USD 20.5 billion or 3.4 months of future imports.

The weighted-average yields of government hryvnia securities dropped in May amid the decrease in the key policy rate seen in late April (by 50 bp, to 17.5% per annum), expectations of further key policy rate cuts, and relatively high demand for hryvnia-denominated domestic government bonds in the first half of May. The UIIR also dropped somewhat, hovering around the lower boundary of the NBU's rates on standing facilities. In April, hryvnia loan and deposit rates showed mixed trends.

Throughout most of May, the hryvnia continued to strengthen gradually amid a significant supply of foreign currency on the FX market. However, deteriorating external financial conditions for emerging markets and increased uncertainty in Ukraine put the hryvnia under depreciation pressure at the end of the month. As a result, in May hryvnia weakened against the U.S. dollar and euro (by about 1.0% mom).

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