

Ukraine: boom over, debts due

The Ukrainian economy grew by some 4% in 2002, well below the torrid 9.1% GDP growth achieved in 2001. Domestic demand remained strong, but foreign demand was weak, especially in the first half. Above-average output growth occurred in petroleum products, food processing, wholesale and retail trade, forest products, machine-building, and transport equipment. Agriculture grew by only 1.9%, below expectations, owing to the high base of 2001 and a slowdown in non-grains. The 2000-01 investment boom faltered in 2002: construction fell 5.8% for the year; real interest rates remained high despite further cuts in the refinancing rate. There are no annual investment figures to date, but gross fixed investment as of September had slowed its rise to 6.2% year-on-year, cf. over 20% in 2001. FDI and privatization revenues were disappointing.

Industrial output rose 7% in 2002; within it, manufacturing was up 8.9%, cf. 14.2% and 17.2% respectively in 2001. Though there was a growth slowdown, it was worse in the first half than the second, and industry managed 9.3% growth in the last quarter year-on-year, as Russian oil revenues continued to be high, and the world economy began to come out of the doldrums. Steel and other metals, after contracting during September 2001-May 2002, picked up in the second half, managing 3.9% growth for the year. Output of the steel industry was a quarter above its 1999 level, though still 35% below the late Soviet peak. Judging by January-October data, metals exports rose over 2%, though this was mainly accounted for by raw steel; steel products, which make up nearly 30% of goods exports, saw sales down over a fifth. The machinery sector increased production by 11.3%, led by machine tools and transportation equipment. Basic oil refining continued its strong rebound, with petrol, diesel and heating oil output up 17-34%.

In agriculture, the bumper harvest of 2001 was nearly equalled in 2002, at 38.8 million t of cereals (after processing), of which grains made 22.5 mn t; yields were the best in eight years. Sunflower output soared 45%. However prices reflected the abundance, with e.g. potato prices falling 42%, and the sector has greatly shrunk in the past decade, so the impact on GDP growth was modest. The Land Code that took effect in early 2002 is bearing fruit, however, even if the long-awaited boom in FDI into e.g. organic farming on Ukraine's world-class *chernozem* has yet to occur on any scale, on account of the business climate in general and, in particular, the very slow planned liberalization of limits on agricultural activity by non-traditional users, such as foreigners.

Total goods exports in dollars grew by 8%, but sales to Russia and the rest of the CIS were down, by 8%, reflecting weaker Russian demand for industrial commodities and grains, and Russian trade restrictions. In euro terms, goods exports to all destinations managed

only a tepid 3.1% rise. Merchandise imports in dollars rose 6%, in euros, 1%. The trade surplus rose substantially and the current account surplus stood at nearly 6% of GDP at yearend according to the IMF, thanks to a stronger services balance, higher remittances, and e.g. WWII compensation payments from Germany and Austria. More than 40% of merchandise exports consisted of steel and steel products, which count as sensitive in the EU, so that despite its proximity, Ukraine trades relatively little with Europe, in a sort of reverse gravity model. WTO accession, hoped-for by end 2004, may help Ukraine sell more to its richest neighbour.

Inflation turned out much tamer in 2002 than expected, and President Kuchma complained of this in firing the head of the National Bank in November. The CPI actually fell between January and December 2002, in part on account of lower food prices; the PPI rose 5.7% on the same basis (3.1% on annual average). The real exchange rate depreciated slightly, so Ukraine's competitiveness improved, especially vis-à-vis Europe; labour costs remain very low compared to neighbours'. With the euro's winter surge, this effect has strengthened, though trade restrictions and anti-dumping actions will likely dampen the impact. The hryvnia may be allowed to depreciate more than the budget assumption of 5.6 UAH to the USD. Though prices were stable in 2002, wages and money incomes grew nearly 20% in real terms for the second year running, and retail trade turnover rose almost 15%. State debt payments of some USD 1.5 billion weigh on the budget. The fiscal system remains a mess, with a doubling of VAT arrears in 2002, government arrears on VAT refunds, myriad exemptions, and fears that either the proposed tax code, the new customs code, or *ad hoc* profits taxes may push business back into the shadows.

Cumulative FDI as of end September 2002 was reported at USD 4.923 billion, about USD 100 per capita. Owing to the low attractiveness of debt-laden privatization objects, the government's revenues from selloffs came in at a tenth of the budget's original projection of them.

In 2003, and indeed 2004-05, the state will have to scramble to meet principal and interest payments on foreign- and domestic-currency debt. Some USD 1.53 billion worth of foreign-currency state borrowing falls due this year (USD 1.02 billion in principal and USD 510 million in interest); that does not include Ukraine's debt to the IMF. Peak months are March and September, in each of which USD 256 million in principal and interest on eurobonds falls due, hopefully to be more than covered by new euroloans in the works, worth up to USD 700 million. Some USD 500 million worth of domestic borrowing also falls due in 2003. The government has many more reserves than in past years, with over USD 4 billion in NBU coffers by yearend. The current account surplus may narrow but remain adequate. Concerns about raising the foreign exchange to meet the higher debt payments are thus mainly fiscal, as opposed to trade-related.

Ukraine's relations with Europe, the US and NATO have been at least temporarily put in the freezer by the scandals around President Kuchma. Even if Kuchma does not step down early, à la Yeltsin, for instance in favour of newly-appointed Prime Minister Yanukovich, the year 2003 marks the beginning of the 'lame-duck' phase of the long Kuchma presidency. By the time a new president takes office in late 2004, Ukraine will have three new EU-member neighbours.

Table UA

Ukraine: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 ¹⁾	2003	2004
									forecast
Population, th pers., end of period ²⁾	50894.0	50499.9	50105.6	49710.8	49291.2	48415.5	48036.6 ^{Oct}	47650	47350
Gross domestic product, UAH mn, nom.	81519	93365	102593	130442	170070	201927	216510	246000	275000
annual change in % (real)	-10.0	-3.0	-1.9	-0.2	5.9	9.1	4.1	4	4
GDP/capita (USD at exchange rate)	872	989	833	633	632	769	842	920	968
GDP/capita (USD at PPP - wiiw)	3330	3630	3630	3710	4050	4580	4890	.	.
Gross industrial production									
annual change in % (real)	-5.2	-0.3	-1.0	4.0	12.4	14.2	7.0	6	7
Gross agricultural production									
annual change in % (real)	-9.5	-1.8	-9.6	-6.9	9.8	10.2	1.9	5	5
Goods transport, bn t-kms	450.3	402.3	391.7	388.0	394.1	393.8	.	.	.
annual change in %	-17.2	-10.7	-2.6	-0.9	1.6	-0.1	3.3	.	.
Gross fixed investment, UAH mn, nom.	12557.0	12437.0	13958.0	17552.0	23629.0	32573.0	19839.0 ^{I-X}	.	.
annual change in % (real)	-22.0	-8.8	6.1	0.4	14.4	20.8	6.2 ^{I-X}	10	15
Construction output total									
annual change in % (real)	-31.0	-9.9	2.7	-8.0	9.1	16.7	-0.7	.	.
Dwellings completed, units	88100	80000	70000	73000	62600	65000	.	.	.
annual change in %	-25.5	-9.2	-12.5	4.3	-14.2	3.8	3.2	.	.
Employment total, th pers., average	23231.8	22597.6	22348.7	21823.7	21268.5	20941.9	20100	20000	.
annual change in %	-2.1	-2.7	-1.1	-2.3	-2.5	-1.5	-4	.	.
Employees in industry, th pers., average ³⁾	4642.0	4273.0	4142.0	3932.0	3445.0	3497.5	.	.	.
annual change in %	-7.8	-7.9	-3.1	-5.1	-12.4	1.5	.	.	.
Reg. unemployed, th pers., end of period	351.1	637.1	1003.2	1174.5	1155.2	1008.1	1034.2	.	.
Reg. unemployment rate in %, end of period	1.3	2.3	3.7	4.3	4.2	3.7	3.8	4	4
LFS - unemployment rate in %, average	7.6	8.9	11.3	11.9	11.7	11.1	9.8 ^{I-X}	10	11
Average gross monthly wages, UAH ³⁾	126.0	143.0	153.0	177.5	230.1	311.1	376.0	.	.
annual change in % (real, gross)	-4.2	-2.1	-3.2	-5.4	1.1	20.7	21.8	.	.
Retail trade turnover, UAH mn	17344	18933	19317	22151	28757	34417	39192	.	.
annual change in % (real)	-5.1	0.2	-6.6	-7.1	8.1	13.7	14.8	.	.
Consumer prices, % p.a.	80.2	15.9	10.6	22.7	28.2	12.0	0.8	10	7
Producer prices in industry, % p.a.	52.1	7.7	13.2	31.1	20.9	8.6	3.1	0	.
General government budget, UAH mn									
Revenues	30218.7	28112.0	28915.8	32876.4	49117.9	53993.0	54371.2 ^{I-XI}	50021 ⁴⁾	.
Expenditures	34182.8	34313.0	31195.7	34820.9	48148.6	55256.6	50542.9 ^{I-XI}	52056 ⁴⁾	.
Deficit (-) / surplus (+)	-3964.1	-6201.0	-2279.9	-1944.5	969.3	-1263.6	3828.3 ^{I-XI}	-2035 ⁴⁾	.
Deficit (-) / surplus (+), % GDP	-4.9	-6.6	-2.2	-1.5	0.6	-0.6	1.8 ^{I-XI}	-0.8 ⁴⁾	.
Money supply, UAH mn, end of period									
M0, Currency outside banks	4041	6132	7158	9583	12799	19465	24064 ^{Nov}	.	.
Broad money	9364	12541	15718	22070	32084	45555	59575 ^{Nov}	.	.
Refinancing rate of NB % p.a., end of period	39.6	34.8	74.2	45.0	27.0	12.5	7.0	.	.
Current account, USD mn	-1185	-1335	-1296	1658	1481	1402	2300	1000	.
Current account in % of GDP	-2.7	-2.7	-3.1	5.2	4.7	3.7	5.7	2.3	.
Gross reserves of NB excl. gold, USD mn ⁵⁾	1960	2341	761	1046	1353	2955	4400	3700	.
Gross external debt, USD mn	8840	9555	11483	12438	10350	12100	10843	10563	.
Exports total, fob, EUR mn ⁶⁾	11357	12550	11283	10856	15771	18159	18700	19600	21000
annual change in %	13.2	10.5	-10.1	-3.8	45.3	15.1	3	5	7
Imports total, cif, EUR mn ⁶⁾	13883	15103	13103	11104	15104	17612	17800	18500	19600
annual change in %	17.3	8.8	-13.2	-15.3	36.0	16.6	1	4	6
Average exchange rate UAH/USD	1.830	1.862	2.450	4.130	5.440	5.372	5.327	5.6	6.0
Average exchange rate UAH/EUR (ECU)	2.322	2.113	2.768	4.393	5.029	4.814	5.030	6.0	6.3
Purchasing power parity UAH/USD, wiiw	0.480	0.507	0.561	0.705	0.848	0.904	0.917	.	.
Purchasing power parity UAH/EUR, wiiw	0.520	0.557	0.615	0.768	0.921	0.980	0.990	.	.

Notes: 1) Preliminary. - 2) In 2001 according to census 5, Dec 2001. - 3) Excluding small enterprises. - 4) Budget passed by Parliament end December 2002. - 5) Useable. - 6) Exports and imports of goods according to customs statistics, adjusted for oil, gas and non-declarable goods. Converted from USD to EUR using the ECB EUR/USD foreign exchange reference rate.

Source: wiiw Database incorporating national statistics; wiiw forecasts.