THE BLEYZER FOUNDATION
Turning Transitions Into Prosperity

Ukraine - Economic Situation
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Economic Growth.

During October 2000, the Ukrainian economy continued to grow at an accelerated pace, against expectations that GDP would slow down. In fact, GDP grew by 6.1% in October 2000 year-to-year. The rate of growth in September 2000 was 3.2% compared to the same month in 1999. For the ten months from January to October 2000, the rate of growth of GDP reached 5.1%, year-to-year. During this ten-month period, nominal GDP amounted to UHA 137 billion or about US$25 billion equivalent.

The industrial sector continued to show the most significant increase in gross value added, at 13.5% in October 2000, year-to-year. For the ten-month period to October 2000, industrial output was 11.9%, compared to 1999. The highest growth rates were experienced by the industries oriented at the domestic market, including textiles and apparel (at 39.6%), wood processing/pulp and paper (at 38.7%), and food industry (at 25%).

For the entire year 2000, both GDP and industrial output will be higher than previously anticipated by the Government, with projected rates of growth at 4-5% for GDP (compared to earlier forecasts of 2.0-3.5%) and 10-11% for industrial output (compared to earlier forecast of 7%).

For year 2001, the Government and other research institutions are anticipating that GDP will grow by 4.5%, with industrial and agricultural output increasing by 8.5% and 5.0%, respectively.

Fiscal Policies.

So far in year 2000, tight financial discipline has kept Ukraine's consolidated fiscal budget close to balance. During the first nine months of the year, the fiscal budget had actually a surplus of UAH 1,700 million (about 1.2% of GDP, using the IMF methodology). Although consolidated fiscal revenues were about 10% below the target level of revenues, expenditures were also cut by over 10% from planned levels to maintain balance.

The fiscal budget for year 2001 is currently under discussions by Parliament. On November 30, Parliament passed the draft 2001 budget law on its second, but not final reading. About two-thirds of a total of 70 budget items were approved, including all the macroeconomic assumptions (GDP growth of 4%, inflation of 13.6% in 2001) and an article stipulating that 20% of revenues collected by oil pipelines will go to the state budget. Parliament increased revenues by less than 1% to UAH 41.6 billion, while retaining deficit-free budget assumption, including UAH 5.9 billion of privatization as revenues. Based on the IMF methodology – which excludes privatization revenues -- the budget would have a deficit of 3% of GDP budget deficit, a level that had been agreed with the last IMF mission. The final third reading vote of the budget in Parliament is currently scheduled for December 7.

Monetary Policies.

Inflation. Since July this year, inflation has been under control, following accelerated inflation rates during the first half of the year. Inflation in November 2000 was only 0.4%. The inflation rate for the five-month period from July to November was 4.3% (equivalent to an annual rate of 10.6%). For the entire period from January to November, inflation was 23.8%, a relatively high rate driven by high inflation during January-June. For the entire year 2000, Ukraine's inflation rate is expected to be about 25%. For year 2001, the Government now anticipates that inflation will be 13.5%, assuming the normalization of lending relations with the international agencies.

The Exchange Rate. During this year, the exchange rate for the Hryvnia has remained relatively stable at around 5.4-5.5 UAH/US$. In fact, in the last 11 months, the interbank Hryvnia rate has declined only 4.5% from 5.2 UAH/USD to 5.4 UAH/USD. This stability follows two years of rapid currency depreciation: the Hryvnia rate dropped 50% in 1999, and it collapsed by 80% in 1998, following the Russian financial crisis. The stability of the Hryvnia during 2000 was due partly by good export performance.

International Reserves. Since the beginning of the year, the level of international reserves has been relatively stable at about US$1.1 billion. This stability was achieved in spite of the fact that the country had to make significant repayments on its foreign debt from its own international reserves.

Government Debt.

In October 2000, Ukraine's Government debt stood at US$13.9 billion, a decline of US$1.4 billion since the beginning of the year. Foreign debt fell by US$2.4 billion to $10 billion, while domestic debt increased by US$1.0 billion equivalent to $3.9 billion.

Ukraine has paid debts to intentional financial institutions without getting any foreign loans since September 1999. In order to serve its international debt, since the beginning of the year, the Government purchased about US$1.3 billion of foreign exchange in the open market, principally during the first-half of the year, which led to high inflation during this period. In the absence of international borrowings, the NBU may have to continue its purchase of foreign exchange in the open market, putting pressures on the inflation rate and on the Hryvnia exchange rate.

During the 2001 budget discussions, the Parliament has set limits on Ukraine's public debt. As of January 1, 2002, foreign debt should be no more than US$10.8 billion and domestic debt should be no more than the equivalent to US$3.9 billion (UAH 14.2 billion in Hryvnia and US$1.3 billion in dollar denominations).

International Trade and Capital.

In the first nine months of 2000, Ukraine's foreign trade turnover totaled US$20.2 billion, an increase of 22.6% year-to-year. The country's trade surplus increased from US$148 million on September 1, 2000 to US$394.7 million on October 1, 2000.

From May 2000 on, monthly exports have exceeded imports by US$200 million on average. From January to September 2000, exports rose 23.9% year-to-year, to US$10.3 billion, largely due to a 50% increase in the export of chemicals and a 40% increase in the export of metals and equipment. Ferrous metals accounted for 36% of overall exports, chemicals for 11%, equipment for 9%, and mineral fuel, oil and oil products for 5.5%.

During the first nine months of the year, imports rose 21.3% to US$9.9 billion. Gas imports, which make up a quarter of overall imports, rose by 9%, and equipment imports, which accounts for 9% of imports, went up 40%.

During 2000, barter operations were reduced. They accounted for 1.7% of exports and 1.8% of imports, compared with 4.3% and 3.4%, respectively, in the first nine months of 1999.

Ukraine's main trade partners were Russia (accounting for 20.2% of exports and 46.8% of imports), Germany (5.2% and 7.6%), the United States (5.8% and 2.5%), Italy (4.1% and 2.5%) China (4.5% and 0.9%), and Poland (3.1% and 2.1%).

Including services, Ukraine has shown even a more favorable balance than with goods alone. The positive balance of Ukraine's foreign trade in goods and services amounted to US$2.0 billion in the first nine months of this year.

Foreign investment in the Ukrainian economy has also increased during year 2000. It reached US$588 million in the first nine months of this year, bringing total foreign investment in Ukraine to US$3.7 billion since independence in 1991. The level of foreign investments so far in year 2000 represents an increase of 18% over the levels achieved in the last two years. The following were the largest investors in Ukraine as of October 1, 2000: the United States — USD 631 million; the Netherlands — USD 357 million; Cyprus — USD 355 million; Russia — USD 294 million; and Great Britain — USD 283 million. The food industry is the largest recipient of Foreign Direct Investments with approximate share of 21%. The rise in foreign investors' activity is mainly explained by the start of large-scale privatization and adoption of more favorable investment legislation.

Multilateral Programs

The Government is dependent on the renewal of lending by the IMF to ensure financial stability in year 2001, given the size of its foreign debt service obligations. IMF lending was suspended in September 1999. Until September 2000, a major bottleneck was the investigation of the claim that the NBU provided false information and misused its international reserves. An international audit carried out by PricewaterhouseCoopers showed that there was not any evidence that Ukraine had misused the funds received from the IMF, but that, indeed, it had overstated the level of NBU currency reserves. This issue was closed in early September 2000, following an early refund by the NBU to the IMF of US$95 million.

Following several IMF missions in the last few months, a final senior IMF mission visited Kiev in November 2000 to review progress made in the implementation of IMF programs of economic reforms. The IMF mission reported that would progress was made on all areas of discussion, and that the IMF lending program would be renewed on December 20, 2000, provided that three conditions are met: (i) Parliament approved a satisfactory budget for year 2001 with a deficit of no more than 3% of GDP; (ii) Parliament approves the Law on Banks and Banking Activities; and (iii)

Government submits to Parliament of the list of enterprises subject to privatization. The Government is confident that the country would be able to address these three issues in the first-half of December 2000. Accordingly, it expects that the IMF Board will make a favorable decision on the revival of the EFF Program and disburse US$250 million by the end of the year.