THE BLEYZER FOUNDATION
Turning Transitions Into Prosperity

Ukraine - Economic Situation

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Economic Growth.

1. After January's GDP upsurge of 9.1%, real GDP growth slowed down somewhat in February 2001, with GDP growing by 6.2%, compared with February last year. During the January-February period of this year, real GDP increased by 7.6% compared to the same period last year, backed by a 16.7% increase in industrial output. These rates give validity to the official Government's forecast of a 4% GDP annual growth rate for this year.

2. During the first two months of the year, Ukraine's industrial output registered the biggest rate of output growth in the Commonwealth of Independent States (CIS). At 16.7%, it compares favourably with those of Kyrgyzstan at 15.4%, Tajikistan at 12.9%, Armenia at 11.4%, Kazakhstan at 9.8%, Azerbaijan at 6.6%, Moldova at 4.5%, Russia at 3.1% and Belarus at 1.8%. Georgia showed a decrease of 13.5%.

Fiscal Policies.

3. During the first quarter of 2001, fiscal revenue targets under Ukraine's consolidated fiscal budgets were fully met. First-quarter revenues are now expected to total US$1.0 billion, which is about US$90 million above the targeted level agreed upon under the program with the International Monetary Fund. Ukraine's state budget revenues in January and February 2001 were 13.3% above the plan. As expenditures were kept under control, the state budget in January-February showed a large surplus amounting to 10% of budget revenues.

4. As of the end of February, the state budget received US$ 110 million from the privatization of state enterprises. These privatization proceeds exceeds the Government's plan of US$90 million for this two-month period. However, the privatization target for the first quarter of the year, at US$210 million will not be achieved, due to the postponement of the privatization 6 oblenergos (regional power companies) to April. It is also doubtful that the privatization targets for the entire year (US$1.1 billion) will be achieved. This will require the Government to cut its planned fiscal expenditures during the rest of the year.

Monetary Policies.

5. During March 2001, the NBU continued tight monetary policies. In fact, money supply (M3) declined slightly during March. During the first three months of the year, money supply increased by 2.2%, while the money base dropped 0.8%. As a result, inflation has been kept under control. Following a high monthly rate of 1.5% in January, inflation went down to 0.6% in February and 0.6% in March. Inflation for the three-month period January-March 2001 was 2.7% (or 11.2% on an annualised basis). If these rates were to be maintained, the Government will be able to achieve its target inflation rate of 13.8% for 2001. Since the beginning of the year, prices for food goods increased by 3.6%, for non-food items - 0.3%, and for services - 1.6%. The exchange rate and the level of international reserves have remained relatively stable during the last months.

International Trade and Capital.

6. In January 2001, Ukraine's foreign trade was favourable. It showed a surplus totalled US$78.3 million, compared to a deficit of US$335.4 million in January 2000. Foreign trade rose 7.1% year-on-year in January 2001 to $2.24 billion. Exports went up 32.1% to $1.16 billion and imports fell 10.9% to $1.79 billion.

7. Of exports 23.1% went to Russia, 6.8% to Greece, 6.4% to Turkey, 5.1% to Italy, 4.7% to Germany, 4.6% to China and 3.7% to the United States. The main imports came from Russia, accounting for 41.2% of overall imports, Turkmenistan (11.4%), Germany (8.5%), Kazakhstan (4.8%), Belarus (2.9%), France (2.6%) and Italy (2.5%).

Government Debt.

8. The World Bank, the International Monetary Fund, and Russia remained Ukraine's largest creditors at the end of last year, holding 60% of its foreign debt. Out of the US$10.3 billion that Ukraine owes, US$2.1 or 20.3% is owed to the World Bank, US$2.0 billion or 20.0% is owed to the International Monetary Fund, and US$1.9 billion or 19.1% is owed to Russia. Ukraine's fourth largest creditor is Germany, with US$349 million or 3.3%, followed by the European Union (with US$319 million or 3.1%), the United States (US$318 million or 3.1%), Turkmenistan (US$282 million or 2.7%), and the European Bank for Reconstruction and Development (US$121 million or 1.2%).

9. Ukraine’s foreign debt service obligations will remain relatively large during 2001 and 2002. It plans to pay US$1.8 billion in 2001 to serve its foreign debt of which about US$650 million would be to the IMF. In 2000, Ukraine paid the IMF $870 million of principal loan and $132 million in interests. In order to serve its foreign debt in a non-inflationary manner, Ukraine must revive its borrowings from the IMF and other multinational institutions.

IMF Program

10. Following the re-initiation of IMF lending to Ukraine in December 2000, the IMF disbursed $248 million. It was also agreed that if economic performance were to progress according to the IMF Program, Ukraine will receive seven quarterly tranches of about

$190 million each, after each successful IMF review mission, for a total of US$760 million in 2001 and US$ 570 million in 2002. The first of the tranche releases of US$190 million was expected to be made at the end of March 2001.

11. An IMF mission visited Ukraine in early February 2001 to review progress under the EFF. The IMF noted that the Ukrainian economy is recovering with a positive GDP growth in 2000 and a positive balance in its current external accounts. However, the IMF mission felt that future recovery was in jeopardy due to the slow implementation in needed economic reforms and conditionality agreed upon under the EFF Program. The IMF has indicated that the Government will need to comply with significant conditionality before it would disburse the March tranche. These conditions include:

- The enactment of adequate policies and procedures to ensure transparency in the privatization of State enterprises.
- The acceleration of financial sector reforms and the restructuring the troubled banks (in particular, the Ukraina Bank and the Savings Bank.)
- The reduction of the sunflower export duty from the current level of 23%, leading to its eventual elimination.
- Progress in the tightening of payment discipline in the energy sector by increasing cash collections.

12. As noted earlier, in year 2001, the Government will need the IMF funds to serve in a non-inflationary manner its US$ 1.8 billion of foreign debt in 2001. The current expectation is that the EFF may be reinitiated in May/June, at the earliest, in a IMF mission expected for May 2001 were to find that the Government has implemented the above-mentioned measures. The Government is aware of the need to maintain the IMF Program alive, given debt service obligations during the year, and has announced that it will be able to meet the IMF conditions by May 2001.

World Bank Programs.

13. On March 22, the World Bank Board of Directors took the decision to grant Ukraine an investment loan worth US$28 million for the development of heat supply system in Sevastopol. The credit will be provided in US dollars at an interest rate of LIBOR+1% for a term of 20 years with a five-year period of grace, and will be repaid since 2006 in equal portions. The WB has already provided a US$ 200 million credit to reconstruct Kyiv's heating system. It has also allocated US$ 18 million to improve energy conservation in Kyiv's buildings. If the IMF Program is in good standing, in May 2001, the WB is expected to approve an adjustment loan for 750 million, of which US$250 million may be available in June 2001.

Bilateral Debt

14. After initial negotiations in Paris on March 6-9, the Paris Club of sovereign creditors decided to delay the consideration of the Ukrainian debt restructuring, worth $1.0 billion. It was reported that this delay was due principally to disagreements among

bilateral agencies on the handling of individual debts. The second round of negotiations with the Paris Club would take place when the bilateral creditors have agreed among themselves on the terms of the restructuring. This is expected to take place in April.