THE BLEYZER FOUNDATION

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Ukraine's External Financing Needs for 4Q 2013 and 2014.

The public sector of Ukraine is not excessively indebted. In fact, total public debt (external and domestic) amounts to $63 million equivalent, or about 33% of GDP, which compares favorably with the average of 35% for emerging countries. The total amount of public external debt of Ukraine (including government and NBU) is also not excessive, amounting to $30 billion or about 16% of GDP. This compares favorably with the average public external debt to GDP ratio of 35% for emerging economies.

On the other hand, private sector debt (banks and corporates) is more substantial at about $104 billion or 56% of GDP. The bulk of this private sector debt (e.g., $83 billion) is due by Corporate borrowers which are quite solvent with significant export revenues. This solvency have allowed them to rollover this debt comfortably. External debt by commercial banks have declined and now amount to $21 billion.

Therefore, Ukraine does not have a debt "solvency" problem per se. Its medium term capacity to serve its debt is adequate. Ukraine's main debt problem is "liquidity", since a large portion of its external debt is short-term. This means that the main issue is the country's ability to rollover current short term repayments or to extend their maturities. The private sector should be able to do this. Therefore, the main liquidity issue in this regard is with external government debt. The government will need to repay about $7.8 billion of principal by the end of next year. In addition to obtaining financing for external government debt, the country requires external resources to its cover large current account deficits which are likely to amount to $15.5 billion in 2014. These two financing gaps are large, given the relatively low level of international reserves of $21 billion. The ability of Ukraine to secure sufficient external resources to cover these gaps will remain the main factor affecting the economic and financial situation of Ukraine in 2014.

Ukraine's ability to meet its external financing needs will depend on various external and internal developments, with the initiation of the Association Agreement with the EU, Russia's response to Ukraine-EU agreement, and resumption of the IMF financing being the most critical ones. Depending on assumptions on these factors, Ukraine's total external financing needs are calculated on the basis of three possible scenarios: Base-line, Optimistic and Pessimistic.

As the tables below shows, under the base-line scenario, Ukraine should be able to secure sufficient foreign currency funds to cover its foreign exchange needs. This would ensure that the exchange rate remains relatively stable, with a maximum devaluation of up to UAH/$ 8.5 by the end of 2014.

Under the optimistic scenario, Ukraine should be able to have sufficient funds to cover its needs and also accumulate about $5 billion of international reserves. The exchange rate would remain stable.

Under the pessimistic scenario, Ukraine will not be able to secure enough financing to cover its requirements. It could face a shortfall of about $32 billion, which exceeds Ukraine's international reserves of $21 billion. This would lead to a default of international obligations both of the government and the private sector. In turn, the exchange rate may depreciate significantly. It should be noted, however, that export oriented industries, such as Agriculture, should not be affected significantly by the devaluation, since export revenues in foreign exchange would not be affected and operating costs may be somewhat reduced. The major impact of the devaluation would be in the accounting of local asset values denominated in dollars. But the market value of these assets would not be affected since revenues, profits and EBITDA would not be negatively affected by a devaluation.

BASE-LINE SCENARIO

The main assumptions for the **base-line** scenario are the following:

1. Ukraine initiates association agreement with the EU in November 2013.
2. Ukraine applies for IMF financing at the end of 2013 but receives the first tranche in 1Q 2014.
3. FDI inflows increase but investors stay cautious in 2014.
4. With IMF financing, Ukraine is able to tap the Eurobond market in 2014.
5. Russia imposes some restrictions on Ukraine's trade but their impact is partially covered by compensatory measures from the EU and/or trade diversification.
6. Population purchases of FX remain moderate (in addition to likely tighter administrative restrictions, sentiments may be positively affected by the presence of IMF program).

Base-line scenario	***2013***	**2014**				
	Q4	Q1	Q2	Q3	Q4	Year
OUTFLOWS						
Current account deficit	-4.0	-5.0	-4.5	-2.5	-3.5	-15.5
Debt repayments						
Government/NBU	-2.0	-1.3	-1.5	-4.3	-0.7	-7.8
IMF	-1.6	-1.2	-1.2	-0.8	-0.4	-3.7
FX domestic securities	-0.5	0.0	-0.2	-0.4	-0.2	-0.8
Eurobonds				-1.0		-1.0
Other (IBRD, bilateral agreements)		-0.1	-0.1	-0.1	-0.1	-0.4
Quasi-government (Naftogaz)				-1.9		-1.9
Banks	-3.0	-3.0	-2.5	-2.0	-4.5	-12.0
Corporations	-10.0	-11.0	-8.5	-9.0	-10.5	-39.0
Population purchases of the foreign currencies	-1.0	-0.8	-0.5	-0.2	-1.0	-2.5
Total outflows	**-20.0**	**-21.1**	**-17.5**	**-18.0**	**-20.2**	**-76.8**
INFLOWS						
FDI	1.2	1.8	1.8	1.5	1.9	7.0
Debt rollover/new borrowing						
Government/NBU	2.0	5.0	3.3	4.0	3.0	15.3
IMF		3.0	1.5	2.0	2.0	8.5
Other	2.0	2.0	1.8	2.0	1.0	6.8
Banks (70% rollover in 4Q 2013, 80% rollover in 2014)	2.1	2.4	2.0	1.6	3.6	9.6
Corporations (105% rollover in 4Q 2013, 115% rollover in 2014)	10.5	12.7	9.8	10.4	12.1	44.9
Total inflows	**15.8**	**21.9**	**16.9**	**17.5**	**20.6**	**76.8**
External financing needs	**4.2**	**-0.7**	**0.6**	**0.5**	**-0.3**	**0.0**

OPTIMISTIC SCENARIO

Main assumptions for the **optimistic** scenario are the following:

1. Ukraine initiates association agreement with the EU in November 2013.
2. Ukraine applies for IMF financing at the end of 2013 and receives the first tranche in 4Q 2013.
3. FDI notably increases in Ukraine.
4. IMF program execution is smooth, despite the forthcoming presidential elections.
5. Russia either does not impose restrictions on Ukraine's trade or their impact is partially covered by compensatory measures from the EU and/or trade diversification.
6. Population purchases of FX are moderate.

Optimistic scenario	***2013***	**2014**				
	Q4	Q1	Q2	Q3	Q4	Year
OUTFLOWS						
Current account deficit	-4.0	-3.5	-3.0	-2.5	-4.0	-13.0
Debt repayments						
Government/NBU	-2.0	-1.3	-1.5	-2.4	-0.7	-5.9
IMF	-1.6	-1.2	-1.2	-0.8	-0.4	-3.7
FX domestic securities	-0.5	0.0	-0.2	-0.4	-0.2	-0.8
Eurobonds				-1.0		-1.0
Other (IBRD, bilateral agreements)		-0.1	-0.1	-0.1	-0.1	-0.4
Banks	-3.0	-3.0	-2.5	-2.0	-4.5	-12.0
Corporations (incl. Naftogaz)	-10.0	-11.0	-8.5	-10.9	-10.5	-40.9
Population purchases of the foreign currencies	-1.0	-0.8	-0.5	0.3	-0.8	-1.8
Total outflows	**-20.0**	**-19.6**	**-16.0**	**-17.5**	**-20.5**	**-73.6**
INFLOWS						
FDI	1.2	2.0	2.0	2.0	3.0	9.0
Debt rollover/new borrowing						
Government/NBU	5.0	1.5	3.0	2.5	3.0	10.0
IMF	3.0	1.5	1.5	1.5	1.5	6.0
Other	2.0		1.5	1.0	1.5	4.0
Banks (70% rollover in 4Q 2013, 90% rollover in 2014)	2.1	2.7	2.3	1.8	4.1	10.8
Corporations (105% rollover in 4Q 2013, 120% rollover in 2014)	10.5	13.2	10.2	13.1	12.6	49.1
Total inflows	**18.8**	**19.4**	**17.5**	**19.4**	**22.7**	**78.9**
External financing needs	**1.2**	**0.2**	**-1.5**	**-1.9**	**-2.1**	**-5.3**

PESSIMISTIC SCENARIO

Main assumptions for the **pessimistic** scenario are the following:

1. Ukraine fails to initiate the association agreement with the EU in November 2013.
2. Ukraine is unable to obtain IMF financing
3. FDI inflows stay subdued.
4. Rollover ratios for corporate debt would be reduced.
5. Russia imposes strict restrictions on Ukraine's trade, but their impact is partially compensated thanks to trade diversification.
6. Population purchases of FX remains high.

Pessimistic scenario	***2013***	**2014**				
	Q4	Q1	Q2	Q3	Q4	Year
OUTFLOWS						
Current account deficit	-4.0	-5.5	-5.0	-4.0	-5.0	-19.5
Debt repayments						
Government/NBU	-2.0	-1.3	-1.5	-4.3	-0.7	-7.8
IMF	-1.6	-1.2	-1.2	-0.8	-0.4	-3.7
FX domestic securities	-0.5	0.0	-0.2	-0.4	-0.2	-0.8
Eurobonds				-1.0		-1.0
Other (IBRD, bilateral agreements)		-0.1	-0.1	-0.1	-0.1	-0.4
Quasi-government (Naftogaz)				-1.9		-1.9
Banks	-3.0	-3.0	-2.5	-2.0	-4.5	-12.0
Corporations	-10.0	-11.0	-8.5	-9.0	-10.5	-39.0
Population purchases of the foreign currencies	-1.0	-1.5	-1.0	-1.0	-1.5	-5.0
Total outflows	**-20.0**	**-22.3**	**-18.5**	**-20.3**	**-22.2**	**-83.3**
INFLOWS						
FDI	1.2	2.0	2.0	1.5	1.5	7
Debt rollover/new borrowing						
Government/NBU	2.0	0.0	1.5	1.0	0.0	2.5
IMF		0.0	0.0	0.0	0.0	0
Other	2.0		1.5	1.0	0.0	2.5
Banks (70% rollover in 4Q 2013 and in 2014)	2.1	2.1	1.8	1.4	3.2	8.4
Corporations (105% rollover in 4Q 2013, 80% rollover in 2014)	10.5	8.8	6.8	7.2	8.4	31.2
Total inflows	**15.8**	**12.9**	**12.1**	**11.1**	**13.1**	**49.1**
External financing needs	**4.2**	**9.4**	**6.4**	**9.2**	**9.2**	**34.2**