Executive Summary

- Russian-backed separatists continue their military confrontations in the Eastern part of Ukraine. Although the intensity of artillery shootings has decreased, it still varies from 5 to 40 per day. The introduction of UN peacekeepers is already preliminary agreed by the major players involved into the conflict resolution, including OSCE, EU and NATO.

- On the reform agenda, Ukraine's international partners have made explicit that further international assistance would depend of the acceleration of the process of reform, including the setting of anticorruption courts, ensuring the independence and viability of the newly established anticorruption agencies, and implementing deeper reform of the judiciary. Recently, President Petro Poroshenko announced that he would submit a new law on the establishment of the Anti-Corruption Court before the end of December.

- In October Ukraine's industrial sector showed signs of recovery, with a growth rate of 0.4% yoy (compared to a decline of -0.3% yoy in January-September). Mining activities continued to be depressed, with quarrying dropping by -8.1% yoy; coal, by -25.1% yoy; lignite, by -0.5% yoy; and metal ore, by -6.4% yoy. On the other hand, in October Ukraine manufacturing grew by 5.7% yoy.

- The consolidated fiscal budget deficit (state and local) for the month of October was at UAH 10.4 billion, reducing the cumulative fiscal surplus from the beginning of the year to UAH 31.2 billion (or a surplus of about 1.3% of period GDP).

- Consumer inflation decelerated from 16.4% yoy in September to 14.6% yoy in October. At the same time, core inflation further expanded, reaching 8.1% yoy.

- In the banking sector, bank deposits in October increased by 10.4% yoy for Hryvnia deposits and by 4.7% yoy for foreign currency deposits. On the lending side, household loans in Hryvnias expanded by 23.6% yoy, whereas corporate loans in Hryvnias increased by 13.4% yoy. The growth of money supply in October was 6.7% yoy.

- During November, the UAH/USD exchange rate saw several reversals of trends. As a result, the UAH/USD exchange rate depreciated by about 1.0% during the month reaching 27.1 UAH per USD by the end of November.

- In October 2017, Ukraine’s current account deficit of the balance of payments declined by 55% mom to USD 408 million. This current account improvement in October 2017 was due to a reduction in the primary investment income account of USD 534 million during the month. Since net financial inflows amounted to USD 563 million in October, they covered the current account deficit and allowed international reserves to increase to USD 18.7 billion by the end of October 2017 (3.7 month of the future imports).

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**Main Macroeconomic Indicators**

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<tr>
<td>GDP, USD billion</td>
<td>163</td>
<td>173</td>
<td>180</td>
<td>130</td>
<td>87</td>
<td>93.4</td>
<td>101.0</td>
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<tr>
<td>Real GDP Growth, % yoy</td>
<td>5.5</td>
<td>0.2</td>
<td>0.0</td>
<td>-6.6</td>
<td>-9.9</td>
<td>2.3</td>
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<tr>
<td>Fiscal Balance (incl. Naftogaz/Pension Fund), % of GDP</td>
<td>-4.3</td>
<td>-5.5</td>
<td>-6.5</td>
<td>-11.7</td>
<td>-2.1</td>
<td>-2.3</td>
<td>-3.5</td>
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<tr>
<td>Public Debt, External and Domestic, % of GDP</td>
<td>36.4</td>
<td>36.6</td>
<td>40.4</td>
<td>69.4</td>
<td>79.1</td>
<td>81.2</td>
<td>78.0</td>
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<tr>
<td>Consumer Inflation, eop, % yoy</td>
<td>4.6</td>
<td>-0.2</td>
<td>0.5</td>
<td>24.9</td>
<td>43.3</td>
<td>12.4</td>
<td>12.5</td>
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<tr>
<td>Hryvnia Exchange Rate per USD, eop</td>
<td>8.0</td>
<td>8.1</td>
<td>8.2</td>
<td>15.8</td>
<td>24.0</td>
<td>27.0</td>
<td>27.8</td>
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<tr>
<td>Current Account Balance, % of GDP</td>
<td>-6.3</td>
<td>-8.3</td>
<td>-9.0</td>
<td>-4.1</td>
<td>-0.2</td>
<td>-4.1</td>
<td>-3.9</td>
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<tr>
<td>FDI, Net Annual Inflow, USD billion</td>
<td>7.0</td>
<td>7.2</td>
<td>4.1</td>
<td>0.3</td>
<td>2.3</td>
<td>3.4</td>
<td>3.0</td>
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<tr>
<td>International Reserves, USD billion</td>
<td>31.8</td>
<td>24.5</td>
<td>20.4</td>
<td>7.5</td>
<td>13.3</td>
<td>15.5</td>
<td>18.5</td>
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<tr>
<td>Public External Debt, USD billion</td>
<td>33.3</td>
<td>32.1</td>
<td>31.7</td>
<td>34.9</td>
<td>42.6</td>
<td>42.5</td>
<td>47.0</td>
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<td>Private External Debt, USD billion</td>
<td>92.7</td>
<td>102.3</td>
<td>110.3</td>
<td>91.2</td>
<td>76.0</td>
<td>69.9</td>
<td>65.0</td>
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**Political and Reform Developments**

Russian-backed separatists continue their military confrontations in the Eastern part of Ukraine. Although the intensity of artillery shootings has decreased, it still varies from 5 to 40 per day. As a result, during November, the number of death casualties among Ukrainian militants reached five.

The resolution of this military conflict remains an important item in international security agendas. Introduction of UN peacekeepers is already preliminary agreed by the major players involved into the conflict resolution, including OSCE, EU and NATO. Although the specifics are still to be discussed the overall expectation among these agencies is that peacekeepers will be present on all territory controlled by separatists.

Fighting corruption continues to be the most important item in Ukraine’s reform agenda. Ukraine's international partners have made explicit that there is a need to accelerate the process of reform, including the setting of anticorruption courts, ensuring the independence and viability of the newly established anticorruption agencies, and implementing deeper reform of the judiciary. The absence of prosecution of top officials accused of corruption is used as a symbol that the existing anti-corruption measures are not working. Recently, President Petro Poroshenko announced that he would submit a new law on the establishment of the Anti-Corruption Court before the end of December. But to register a new bill, the Ukrainian parliament will have to withdraw two other draft bills which were criticized by the Venice Commission. During the month, there were also some attempts by some members of Parliament and other law enforcement institutions to challenge the work and independence of the newly created anticorruption institutions. These challenges have been rejected by both international agencies and civil society representatives. The IMF is delaying consideration of its tranche release until anti-corruption issues are addressed.

During the past month, amendments to the pension law were introduced. These amendments cut back on early retirement packages and increased the length of service before pension payments could be claimed from 15 years to 25 years. It also increased pension payments in the future. But last minute amendments withdrew the planned increases in pension age eligibility, retaining the current eligibility age of 60 years old for men and 58 years old for women.

At the end of November, President Poroshenko signed a law introducing amendments to the Judiciary system. This law introduced new rules of litigation in civil, economic, administrative proceedings, as well as some changes in the rules of criminal processes.

**Economic Growth**

In October Ukraine's industrial sector showed signs of recovery, with a growth rate of 0.4% yoy (compared to a decline of -0.3% yoy in January-September). Mining activities continued to be depressed, with quarrying dropping by -8.1% yoy; coal, by -25.1% yoy; lignite, by -0.5% yoy; and metal ore, by -6.4% yoy. On the other hand, in October Ukraine manufacturing grew by 5.7% yoy, due to the expansion of the following sub-sectors: chemical products (by 38.9% yoy); furniture and other manufacturing (21.8% yoy); basic pharmaceutical products (8.8% yoy); textiles (8.7% yoy); rubber, plastic and other non-metallic mineral products (5.5% yoy); foodstuffs production (3.8% yoy); machinery and equipment (3.8% yoy); and metallurgy (3.3% yoy); and
wood products (2.3% yoy). However, the following subsectors continued to decline: production of coke, refined petroleum products (by -10.3% yoy) and electricity, gas, steam with air conditioning supply (by -7.6% yoy).

In October, Ukraine’s retail trade turnover continued to expand, though at a lower rate of 4.2% yoy (compared to 8.2% yoy in Jan-Oct). Similarly, construction output increased by 13.1% yoy (compared to 23.4% yoy in January-October). On the other hand, due to bad weather, agriculture production continued to shrink by -0.9% yoy in October (compared to a decline of -2.3% yoy in Jan-Oct).

In terms of main industrial groups, in October 2017, the largest increase took place in investment goods (which increased by 12% yoy), followed by consumer durables (10.7% yoy), short-term consumer goods (4.4% yoy), and goods of intermediate consumption (0.4% yoy).

With regard to the regional distribution of industrial production, the main output increases took place in the following regions: Ivano-Frankivsk (16.1% yoy), Vinnitsa (11.2% yoy), Liv (11.1% yoy) Zakarpattya (9.2% yoy), Zaporizhzhya (9.1% yoy), Zhytomyr (8.5% yoy), Odesa (8.1% yoy), Chernivtsi (6.6% yoy), Poltava (5.7% yoy), Kyiv (4.9% yoy), Sumy (4.3% yoy), Volyn (3.4% yoy), Dnipropetrovsk (3.1% yoy), Ternopil (1.5% yoy), Rivne (1.3% yoy), Cherkasy (0.6% yoy), Kharkiv (0.3% yoy), Chernihiv (0.1% yoy), respectively, in October 2017.

Negative growth rates in industrial output took place in the following regions: Luhansk (-55% yoy), Donetsk (-14.8% yoy), Kyiv city (-6.4% yoy), Khmelnytskyi (-4.7% yoy), Kirovohrad (-3.6 yoy), Mikolayiv (-1.9% yoy), and Kherson (-0.6% yoy).

**Fiscal Policy**

The state fiscal budget was executed with a deficit of UAH 13.6 billion in October. This deficit is lower compared to September’s deficit. On the other hand, the cumulative fiscal balance of the local budgets returned to positive territory (UAH 3.2 billion). Thus, the consolidated budget deficit (state and local) for the month was at UAH 10.4 billion, reducing the cumulative fiscal surplus from the beginning of the year to UAH 31.2 billion (or a surplus of about 1.3% of period GDP).
State budget revenues grew by 10.2% yoy in October. The deceleration in growth was due to a decline in the nontax revenues. At the same time, tax revenues also posted some deceleration in growth (to 26.5% yoy). This 26.5% yoy growth was supported by high receipts from excise taxes, VAT (mainly on imported goods), and also international trade taxes thanks to higher imports and depreciation of hryvnia. Despite this deceleration in growth of the state budget revenues, the cumulative consolidated budget revenues grew at high rate of 39.7% yoy in January-October.

State budget expenditures grew rapidly in October. They increased by 42.9% yoy on the back of significant growth in social security expenditures. This was the result of return to growth in transfers to the Pension Fund (28.1% yoy) after six month of declines. There was also an increase in expenditures on servicing of internal public debt. Expenditures on both purchases of goods and services and capital expenditures observed high growth in October. Growth of payroll expenditures and expenditures on current transfers saw some deceleration in the reporting month. The cumulative consolidated budget expenditures posted accelerated growth of 23.5% yoy over ten months of the year.

**Monetary Policy**

**Inflation.** Consumer inflation decelerated from 16.4% yoy in September to 14.6% yoy in October. At the same time, core inflation further expanded, reaching 8.1% yoy.

Deceleration in consumer inflation was the result of lower increases in several important major groups of goods and services. In particular, the growth of housing and utility tariffs decelerated by 8.0 pp to 15.2% yoy, while growth of food prices decelerated by 0.8 pp to 18% yoy. These decelerations in prices were partially offset by accelerated increases in prices of transport (from 12.6% yoy to 14.4% yoy), communication (from 9.7% yoy to 10.6% yoy), and healthcare (from 5.8% yoy to 6.4% yoy). Other major groups of goods and services saw either small or no changes in dynamics of their prices in October. Despite some improvements in price developments, we maintain our forecast for inflation unchanged at 12.5% yoy for 2017.

**Banking Sector.** In October bank deposits increased by 10.4% yoy for Hryvnia deposits and by 4.7% yoy for foreign currency deposits. These rates were lower than in September due to lower rates of growth in corporate sector deposits. Household deposits saw little or no changes during the month. National currency corporate deposits expanded by 5.0% yoy which is a 2.1 pp lower as compared to the previous month. Growth of foreign
currency corporate deposits denominated in USD was 2.4 pp lower at 4.7% yoy.

On the banking lending side, the corporate sector reported deceleration in growth of national currency corporate loans from 20.0% yoy to 13.4% yoy, while the decline of foreign currency corporate loans decelerated from 22.0% yoy to 17.0% yoy. The household sector observed notable changes only in the national currency loans with acceleration in growth to 23.6% yoy.

The increase in cash resources and in balances at the correspondent accounts of banks led to an increase in the monetary base of 0.9% mom and acceleration in its over-year growth to 6.2%. At the same time, money supply remained almost unchanged in monthly terms as a moderate increase in cash outside banks was partially compensated for by the decline in deposits. Thus, the year-over-year growth of money supply also remained almost unchanged at 6.7%.

**Hryvnia Exchange Rate.** As the Hryvnia depreciation trend continued during the first few trading sessions in November, the NBU decided to draw excessive hryvnia resources out of the market and issued certificates of deposits. This, together with the decreased demand for dollar on the side of banks with foreign capital led to appreciation of the exchange rates until November 10th. Then, the exchange rate remained relatively stable until November 20th. However, another tranche of the VAT reimbursements terminated the sideways trend and caused another depreciation. The Thanksgiving Day celebrations in the US and increased demand for dollar on the side of banks with foreign capital for dividends repatriation purposes also contributed to the exchange rate depreciation until the end of the month. Overall depreciation over the month was less than 1% to 27.1 UAH/USD.

**International Trade and Capital**

According to the latest NBU’s report, the deficit in Ukraine’s current account of the balance-of-payments declined by -55% on a month-to-month basis, to USD 408 million in October 2017 (compared to a deficit of USD -901 million in Sept 2017). The cumulative deficit of the current account in Jan-October 2017 shrank by 13.8% yoy to USD 3.3 billion (or 3.9% of period GDP).

The current account improvement in October 2017 was due to a reduction in the primary investment income account of USD 534 million during the month. On the other hand, the deficit in the merchandise trade account increased from USD -638 million to USD -746 million, due to a faster rate of growth of merchandise imports.
(5.3% mom) than exports (2.7% mom).

On a year-to-year basis, merchandise exports increased by 16.6% yoy, reaching USD 3,523 million in October 2017. The merchandise products that had the highest impact on export growth included: agriculture exports, which represented 46% of total exports (reaching USD 1.6 billion, growing at 11.6% yoy); ferrous and nonferrous metals, whose share amounted to 24% of the total (USD 853 million, 23.4% yoy); mineral products, with a share of 9% of exports (USD 302 million, 50.7% yoy); chemical products, with a share of 6% (USD 197 million, 36.4% yoy), and industrial goods, with a share of 2% (USD 53 million, 29.3% yoy). The share of machinery and equipment fell by 2.3% to 7.0% of the total amount in October (USD 236 million, -12.7% yoy).

On the import side, the largest share of imported products in October were as follows: machinery and equipment, with a share of 27% of total imports (USD 1.23 billion, growing by 33% yoy); mineral products, with 24% share (USD 1.1 billion, 30.3% yoy); chemicals products, with a 20% share (USD 883 million, 29.4% yoy), and agricultural products, with a share of 8% (USD 381 million, 17.7% yoy).

Regarding the geographical orientation of exports, in January-October 2017, Ukrainian exports to Europe increased by 32.5% yoy to USD 11.6 billion and now represent 36% of the total exports. At the same time, exports to the Russian Federation fell by 0.6% to a share of 8.6% total exports. Asia foreign trade with Ukraine declined by -2.3% to a 32.5% share of total amounts exported.

In October the current account deficit of USD 408 million was fully covered by financial inflows of USD 563 million, principally to local commercial banks. As a result, the overall consolidated balance-of-payments showed a surplus of USD 155 million (compared to USD $ 91 million in Oct 2016). International reserves grew to USD 18.7 billion, enough for 3.7 months of future import requirements.