FINANCIAL CRISIS INDICATORS AND UKRAINE SITUATION

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By mid-2008, most financial crisis indicators for Ukraine had deteriorated markedly. This deterioration indicates that Ukraine is very vulnerable to a financial crisis in the near future. The indicators are as follows:

CURRENT ACCOUNT INDICATORS

1. Adverse movements in exports/imports (deterioration of trade account in the last 12 months)

   In Jan-May 2008, the merchandise trade deficit deteriorated to $8.8 billion, compared to $3.7 billion for the same period in 2007.

2. Large deterioration in the ratio of current account deficit to GDP (beyond the norm of 3%)

   In Jan-May 2008, the CA deficit was also twice as large as in 2007, reaching $6.2 billion or 9% of period GDP. This gap was covered by FDIs ($4 billion) and foreign borrowings by private sector. Banks have been successful in bringing short term debt.

3. Terms-of-trade deterioration (change in the ratio of export/import prices-based on GDP deflators)

   In 2007 and 2008, the terms of trade improved.

4. Large move in real exchange rates (in last 12 months)

   According to the NBU, real effective exchange rate (REER) appreciated by 6.3% for January-May 2008; according to the IMF, REER is expected to appreciate by about 17% in 2008 vs. 2.6 appreciation in 2007.
CAPITAL ACCOUNT INDICATORS

5. Large increase in the ratio of external debt to GDP
   Public external debt has been stable, but private external debt has increased from $17 billion in Jan 2005 to $77 billion now. Total external debt is now 61% of 12-month GDP.

6. Large increase in short-term debt (% increases in the last 12 months)
   The total stock of short term debt has increased from $10 billion at the beginning of 2005 to $26 billion now. If we include the short-term portion of long term external debt (as many countries do), the real amount to short term debt is about 45 billion.

7. Large increase in the ratio of short term debt to international reserves (beyond the norm of 1.0)
   Ratio of short-term debt (incl. Inter-company lending) to international reserves was 0.8 at the end of 2007 and grew to 0.9 at the end of March 2008. According to external debt methodology, classification of the external debt by short- and long-term is made at the moment of contracting the debt. In we include the short term portion of LT debt, the actual ratio is about 1.3, exceeding 1.0.

8. Quick drop in international reserves (below 3 months of imports)
   International reserves have continued to grow to $35 billion at the end of June 2008.

9. Large drop in net capital inflows (Portfolio inflows or FDIs)
   FDIs are high at $4 billion for Jan-May 2008. But Portfolio inflows declined from $1.8 billion in Q1-2007 to $220 million in Q1-2008.

FINANCIAL SECTOR INDICATORS

10. Large money supply increases and large increases relative to GDP and international reserves
    M3 increased by 45% in 2007. M3/GDP = 54% in June 2008;
    M3/International reserves = 258% at the end of June 2008
11. Excessive rate of growth of bank credit (in excess of 15% pa) or in ratio of bank credit/GDP
   Bank credit has been growing by 70% pa. It was at 60% of GDP at the end of 2007; 61.7% of GDP at the end of June 2008.

12. Deterioration in the level of non-performing assets to total assets (NPA/TA beyond 10%)
   According to the IMF, if we were to include sub-standard loans, the level of non-performing loans would be about 13% of assets.

13. Other erosion in the banks’ profits or capital base
   Not available

14. New evidence of inadequacies in bank supervision
   Loan classification standards and provisioning depart from international practice.

15. Deterioration in the Spread of External Bonds (beyond the overall market changes)
   The spread of Ukrainian bonds in the EMBI deteriorated from 250 basis points in mid 2007 to 480 bp in June 2008.

16. High ratio of fiscal deficits to GDP (beyond the norm of 3%)
   No problem. In 2007 consolidated fiscal deficit = 1.1% of GDP. For January-May 2008 consolidated fiscal balance was in surplus of 3.4% of period GDP. However, consolidated budget expenditures grew by nominal 47% yoy with capital expenditures increasing by 12% yoy, while transfers to the population grew by 54% yoy (state budget expenditures grew by 49% yoy with capital expenditures declining by 8.5% yoy and transfers to the population growing by almost 70% yoy) – everything in nominal terms.

REAL SECTOR INDICATORS

17. Large declines in asset prices, particularly real estate prices and stock prices
   PFTS index declined by 40% year-to-date as of May 2008

18. Large increase in the number of corporate losses or bankruptcies
   Not available

19. Deterioration in the rates of growth of GDP, Industry and/or Electricity Consumption.
   Real GDP growth has been decelerating in the first five months of 2008.