

# ICPS newsletter

## Experts again dampen their economic growth forecast

**Following the Q3'02 results, ICPS' consensus forecast of GDP growth fell from 4.9% to 4.4% for 2002 and from 5.3% to 4.4% for 2003. At the same time, in comparison to the previous forecast experts expect a better foreign trade balance, lower interest rates on commercial bank loans, and a deceleration of the nominal hryvnia depreciation**

The aim of the quarterly seminar on macroeconomic forecasting is to exchange information between major forecasting organisations, and to determine average forecast values for the main economic growth indicators. On October 25, experts from the Ministry of Economy and European Integration of Ukraine, the Ministry of Finance of Ukraine, the National Bank of Ukraine, the Institute of Economic Forecasting of the National Academy of Sciences of Ukraine, the International Monetary Fund, the Institute of Economic Research and Political Consultations, the ING Barings Bank, and International Centre for Policy Studies presented and discussed their forecasts for Ukraine's economic growth. The discussion organised by the Ministry of Economy and European Integration and Support for Economic and Fiscal Reforms project.

### Changes from the previous forecast

The major changes compared to the July forecast are following:

- Anticipated GDP growth dropped by 0.5 percentage points (p.p.) in 2002 and by 0.9 p.p. in 2003. According to the consensus forecast, this indicator will amount to 4.4% in both 2002 and 2003, due to the diminished investment forecast;
- The forecast inflation rate dropped by 3.3 p.p. and 2.4 p.p., respectively, and will come to 0.7% and 7.1% in 2002 and 2003. The 2002 forecast was improved by the increased real demand for money, a steady hryvnia exchange rate, and deflation, which has been maintained during the three quarters;
- The improved current account balance was one of the factors prompting an increase in the forecast indicators for the NBU's international currency reserves (to 4,230

million USD in 2002 and 5,069 million USD in 2003) and for lower hryvnia depreciation (average exchange rate of 5.34 UAH/USD and 5.52 UAH/USD in 2002 and 2003, respectively);

- A more stable hryvnia and a stimulating NBU policy allowed the forecast of a more rapid shrinkage of commercial banks' loan rates than estimated in the July forecast (21.8% and 19.5% in 2002 and 2003, respectively);
- The previous forecast for budget expenditures to exceed revenues was changed to a surplus of the Consolidated Budget for 2002 and 2003, given worse expectations with regard to borrowing.

### Assumptions

The consensus forecast was based on the following major assumptions, on which most seminar participants agreed:

#### Foreign trade:

- Gradual acceleration of world economic growth;
- Diversification of markets for Ukrainian products.

#### Real sector:

- Raised tariffs on natural monopolies (electricity, transport, housing utilities);
- Capital outflows from Ukraine;
- Small volumes of foreign direct investment in 2003–2004.

#### Monetary policy:

- Thanks to the NBU's policy, a stable real effective exchange rate with slow nominal depreciation of the hryvnia against the dollar;
- Lending volumes growing while bank rates are falling;
- NBU reserves growth, though at slower rates than in 2002;

- Improvement of the money aggregate structure, following a soft monetary policy;
- Consolidation of public trust in bank system, expansion of non-cash payments, and savings growth.

#### Fiscal policy:

- Reduction of the personal income tax;
- Holding to the debt repayment and servicing schedule;
- Continuing cooperation with international financial organisations.

### Forecast risks

#### Positive:

- Formation of an effective parliamentary majority and consensus of political powers regarding economic reforms;
- Transparent competition between political powers regarding the quality of economic policy.

#### Negative:

- Sharp deterioration of the global economic situation;
- Growth of world prices on oil and gas;
- Ukraine's economic isolation by the introduction of sanctions by the FATF, UN, or the USA;
- Budget financing at the expense of NBU emissions, and failure to maintain a reasoned exchange rate policy.

### Divergence in experts' opinions

The October discussion on Ukraine's economic development forecast revealed a divergence in the forecasts for consumption and foreign trade. Some experts forecast accelerated consumption, given their assumption regarding the impact a lower of personal income tax rate. Others believed that the deterioration of consumer confidence would negate the effect of lowering the tax rate, and that consumption would slow down. Similarly, some experts thought that accelerated GDP growth in Ukraine's trading partners would increase Ukrainian exports; meanwhile, others

foresaw that protectionism would limit the positive impact of this factor. ■

The International Centre for Policy Studies has been producing quarterly forecasts of

Ukraine's economic growth since 1997. ICPS' economic development forecast for 2002–2003 can be accessed on the ICPS web-site: [http://www.icps.kiev.ua/ukr/forecast\\_2002-2004.html](http://www.icps.kiev.ua/ukr/forecast_2002-2004.html).

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## Comparative table of macroeconomic forecasts for 2002–2003

Indicator	Average value		ICPS indicator		Indicator	Average value		ICPS indicator	
	2002	2003	2002	2003		2002	2003	2002	2003
<b>Real sector</b>	<b>(mill UAH)</b>				<b>Public finances*</b>	<b>(mill UAH)</b>			
Nominal GDP	216,066	240,995	213,100	232,700	Total revenues	59,581	61,529	59,670	60,500
Consumption	171,335	192,788	157,411	165,000	Total expenditures	58,388	61,117	58,600	60,040
private	125,163	142,383	116,040	123,000	Overall balance	1,191	412	1,070	460
public	45,476	49,665	41,371	41,900	<i>Financing items</i>	298	1,103	—	—
Investment	42,017	47,553	40,747	42,900	Privatisation	1,395	2,049	1,500	2,000
Gross accumulation of fixed capital	43,528	48,552	—	—	Domestic borrowing	522	-201	—	—
private	39,219	43,253	—	—	Foreign borrowing	-2,275	-787	-2,100	-860
public	5,686	5,316	—	—	<b>Public finances*</b>	<b>(% of GDP)</b>			
Net exports of goods and non-agency services	3,344	2,249	5,117	1,938	Total revenues	27.7	25.8	28.0	26.0
Gross national savings	53,936	58,705	—	—	Total expenditures	27.2	25.7	27.5	25.8
<b>Real sector</b>	<b>(index, year-over-year)</b>				Overall balance	0.6	-0.0	0.5	0.2
Real GDP	104.4	104.4	104.3	103.5	<i>Financing items</i>	-0.2	0.4	—	—
Consumption	105.6	105.2	105.8	104.8	Privatisation	0.66	0.88	0.7	0.9
private	107.3	106.5	107.0	106.0	Domestic borrowing	0.25	-0.1	—	—
public	102.5	101.4	102.2	101.2	Foreign borrowing	-1.1	-0.4	-1.0	-0.4
Investments	103.6	105.9	106.0	106.5	<b>Money and credit</b>	<b>(mill UAH)</b>			
<b>Inflation</b>	<b>(index)</b>				Monetary base, year-end	31,536	39,182	31,750	40,200
GDP Deflator (average annual)	102.7	106.8	101.2	105.5	Dec. to previous Dec., %	36.0	23.9	38.0	27.0
CPI (average annual)	100.9	106.3	100.9	105.3	Money supply (M3), year-end	62,672	79,131	62,850	80,400
Dec. to previous Dec.	100.7	107.1	100.0	106.5	Dec. to previous Dec., %	38.1	27.1	38.0	28.0
<b>External Sector</b>	<b>(mill USD)</b>				NBU discount rate, %, average annual	8.0	7.8	8.0	7.5
Current account	1,749	1,277	2,030	1,430	Average weighted interest rate on commercial bank hryvnia loans, %, average annual	21.8	19.5	19.0	15.0
Export volumes	20,871	21,650	22,350	23,250	NBU international reserves, mill. USD	4230	5,096	4,585	5,500
Import volumes	-20,341	-21,429	-21,390	-22,890	<b>Social indicators</b>	<b>(thousands of people)</b>			
Revenues balance	-431	-547	-680	-710	Population	48,068	47,692	48,100	47,600
Official transfers (net)	1,723	1,658	1,750	1,780	% change over previous year	-0.9	-0.4	-1.2	-1.1
Capital account	-1,053	-600	-400	-150	Number of employees enrolled in all sectors of economic activities, year-end	20,734	20,684	—	—
FDI	587	678	500	500	% change over previous year	0.9	-0.2	—	—
<b>External Sector</b>	<b>(% of GDP)</b>				Number of registered unemployed, year-end	1,033	1,073,1	—	—
Current account	4.3	2.9	5.1	3.4	registered unemployment, year-end, %	3.8	3.9	4.0	4.0
Export volumes	51.6	49.7	55.9	54.6	Average wage, UAH	365.4	412.6	372.0	416.0
Import volumes	50.3	49.2	-53.5	-53.7	Cash disposable incomes of population, billions UAH	140.3	146.5	—	—
Revenue balance	-1.1	-1.3	-1.7	-1.7	Cash disposable incomes of population, % change over last year	13.9	11.2	20.0	7.0
Official transfers (net)	4.3	3.8	4.4	4.2					
Capital account	-2.6	-1.4	-1.0	-0.4					
FDI	1.4	1.6	1.3	1.2					
<b>Exchange rate,</b>	<b>UAH/USD</b>								
Average annual	5.34	5.52	5.33	5.46					
Year-end	5.36	5.62	5.34	5.55					

\* IMF methodology

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