

ICPS newsletter[®]

Top economists upgrade forecasts for 2004-2005

Real GDP should grow 9.7% in 2004, while 2005 should see a 7.7% rise: such are the results of a consensus forecast produced by top analysts of Ukraine's economy. The earlier forecast has been revised upward for most macroeconomic indicators. The reason behind this improved forecast is a better-than-expected economic dynamic during the first five months of 2004. The only exception is the Producer Price Index

With the support of the Ministry of Economy and European Integration, an expert forecast was carried out for the macroeconomic situation in Ukraine in 2004–5—the second since the beginning of the year. Using data and assumptions, participants—representatives of government and non-governmental institutions, international organizations and business—developed the latest consensus forecast for Ukraine's economic development.

Most indicators are adjusted upward

Compared to data for the previous forecast produced in February 2004, economists upgraded most of the basic macroeconomic indicators. The average value of real GDP growth went up 1.9 percentage points in the 2004 forecast and 1.2 percentage points in the 2005 forecast, for a total growth of 9.7% and 7.7%.

Both the revenue and expenditure sides of the Budget are expected to expand, given the stronger economic dynamic in 2004 and the expected Budget spending spree before the presidential election. Still, experts say that lower tax rates should somewhat cut redistribution of GDP via the Budget (see **TABLE 1**).

As before, the key driver of speedy economic growth is a favorable situation on foreign markets. Experts have adjusted upwards their foreign trade forecasts and expect a larger influx of hard currency in the form of foreign direct investments (FDI). This favorable situation and current trends on forex market make it possible to presume that the UAH/USD exchange rate will remain at the 5.32/1 level throughout 2004–5.

Experts have also upgraded expectations for the economy's monetization and say that the threat of inflation will encourage banks to be cautious in lowering interest rates on loans. The forecast average interest rate for 2004 is 17.3%, and 15.9% in 2005, in contrast to the 15% and 14.5% predicted in February.

Inflation poses a threat

The forecast for the growth of the Consumer Price Index in 2004 (December on December) has been lowered from 7.2% to 6.7%, though same indicator for 2005 has been increased from 6% to 6.7%. This rise resulted from the anticipated impact on the consumer market of a growing Producer Price Index—which rose significantly in the first months of 2004. In December 2004, this indicator is expected to hit 15.5% and then plunge to 6.8% by December 2005. Still, ICPS economists expect this Producer Price Index to continue to rise, about 20% in 2004.

Favorable conditions dominate

Among the assumptions underlying these economic forecasts, the most frequently mentioned are:

- the persistent favorable external situation for Ukrainian exports, the granting of market economy status by the EU and the US, and accession to the WTO in 2005;
- growing consumption, a gradual loosening of price controls, and rising rates for residential services in 2005;
- continuing high inflows of hard currency, stability in the UAH/USD

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exchange rate, growing foreign currency reserves at the NBU, and a slowdown in the lowering of interest rates by commercial banks.

The key risk to this forecast is escalating inflation. During their discussions, economists expressed concern that the risk of inflationary

shock is far greater than the results of the average forecast might suggest. Among other risks, these experts also mentioned the possibility of a steep change on world markets and the delay of investment decisions prior to the presidential election. ■

More information about materials from these quarterly macroeconomic forecasting seminars can be seen on the web-site of the Ministry of Economy and European Integration

(<http://me.kmu.gov.ua>), in the "Economic Situation and Forecasts" section.

This seminar was held with the support of the Millennium Development Goals Project under the UNDP. Forecasts were submitted by the following organizations: the Support Group at the Coordination Council on Financial Sector Policy, the Institute for Economic Research and Policy Consulting, the Institute for Economic Forecasting under the National

Academy of Sciences of Ukraine, Dragon Capital, GfK-USM, Alfa and Co., the International Centre for Policy Studies, the Ministry of Economy and European Integration, the National Bank of Ukraine, the IMF representative office in Ukraine, and the World Bank representative office in Ukraine.

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Table 1. Average macroeconomic forecast for 2004–2005

Index	2004		2005		Index	2004		2005	
	Consensus forecast	ICPS forecast	Consensus forecast	ICPS forecast		Consensus forecast	ICPS forecast	Consensus forecast	ICPS forecast
Real sector (mn UAH)					Exchange rate, UAH/USD				
Nominal GDP	317,151	↑ 315,300	363,070	↑ 357,500	average	5.33	↓ 5.33	5.32	↓ 5.32
Consumption	241,794	↑ 241,100	275,858	↑ 273,200	year-end	5.32	↓ 5.32	5.32	↓ 5.30
private	157,476	↓ 177,500	207,445	↑ 203,700	Public finance (mn UAH)				
public	62,215	↑ 63,600	68,381	↑ 69,500	Total revenues	84,986	↑ 85,131	96,888	↑ 98,313
Investment	66,163	↑ 69,100	78,116	↑ 80,500	Total expenditures	87,626	↑ 89,861	98,648	↑ 100,100
Gross accumulation of fixed capital	65,572	↑ —	78,106	↑ —	Overall balance	-2,640	↑ -4,730	-1,760	↓ -1,788
private	58,752	↑ —	68,171	↑ —	<i>Financing items</i>				
public	5,716	↓ —	8,950	↑ —	Privatization	3,383	↑ 3,000	2 286	↓ 1,600
Net export of goods and non-agency services	9,391	↑ 10,100	9,063	↑ 9,000	Domestic borrowing	-320	↓ 100	-474	↑ -600
Gross national savings	83,437	↑ —	95,386	↑ —	International borrowing	1,086	↓ 1,600	691	↓ 800
Real sector (index, year-on-year)					Public finance (% of GDP)				
Real GDP	109.7	↑ 110.0	107.7	↑ 108.0	Total revenues	26.8	↓ 27.0	26.7	↓ 27.5
Consumption	110.8	↑ 112.0	108.7	↑ 108.0	Total expenditures	27.6	↓ 28.5	27.2	↓ 28.0
private	111.9	↑ 112.0	108.5	↑ 109.0	Overall balance	-0.8	↑ -1.5	-0.5	= -0.5
public	106.9	↑ 112.0	104.7	↑ 104.0	<i>Financing items</i>				
Investment	112.1	↑ 114.0	112.1	↑ 114.0	Privatization	1.1	↑ 1.0	0.6	↓ 0.4
Gross national savings	121.7	↑ —	111.1	↑ —	Domestic borrowing	-0.1	↓ 0.0	-0.1	↑ -0.2
Inflation (index)					Foreign borrowing				
GDP Deflator (average annual)	109.4	↑ 108.5	106.4	↑ 105.0		0.3	↓ 0.9	0.2	↓ 0.4
CPI (average annual)	107.2	↓ 107.0	106.5	↑ 107.0	Money and credit (mn UAH)				
Dec. on Dec.	106.7	↓ 106.0	106.7	↑ 107.0	Monetary base, year-end	50,727	↑ 54,000	62,813	↑ 68,000
PPI (average annual)	116.7	↑ 118.0	108.8	↑ 110.0	Dec. on Dec., %	26.5	↑ 35.0	23.8	↑ 25.0
Dec. on Dec.	115.5	↑ 120.0	106.8	↑ 108.0	Money supply (M3), year-end	129,871	↑ 135,000	170,336	↑ 178,000
External Sector (mn USD)					Dec. on Dec., %				
FDI	1,350	↑ 1,600	1,522	↑ 1,800		36.6	↑ 42.0	31.2	↑ 32.0
Current account balance	3,307	↑ 3,400	2,922	↑ 3,000	Average weighted interest rate on commercial hryvnia loans, % pa				
Export volumes	35,143	↑ 35,700	38,933	↑ 38,400		17.3	↑ 17.0	15.9	↑ 16.0
Import volumes	33,525	↑ 33,800	37,679	↑ 36,700	NBU international reserves, mn USD				
Revenue balance	-424	↑ -550	-424	↑ -520		8,729	↑ 10,000	10,639	↑ 13,000
Official transfers (net)	2,114	↑ 2,000	2,092	↑ 1,800	Social indicators				
External Sector (% of GDP)					Population, millions				
FDI	2.3	↑ 2.7	2.2	↓ 2.7		47.4	= 47.3	47.1	= 47.1
Current account balance	5.6	↑ 6.1	4.3	↑ 4.5	% change over previous year				
Export volumes	59.0	↑ 64.6	57.0	↑ 61.4		99.4	= 99.2	99.4	= 99.6
Import volumes	56.3	↑ 61.1	55.2	↑ 58.6	Average wage, UAH				
Revenue balance	-0.7	↑ -1.0	-0.6	↑ -0.8		575.0	↑ —	658.7	↑ —
Official transfers (net)	3.5	= 3.6	3.1	↑ 2.9	% change over previous year				

↓ – higher/lower indicator, compared to the consensus forecast in February 2004.

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