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Inflation spurs consumers to buy more

Starting in March 2004, consumer confidence has been largely positive in Ukraine. In June 2005, the Consumer Confidence Index (CCI) stood at 105.2, 2.1 points below the value registered during the previous poll in March 2005. Although economic expectations deteriorated, the poll registered a considerable improvement in the current financial standing of Ukrainians, in particular a growing propensity to consume. The latest issue of the Consumer Confidence quarterly will be released this week

Having reached a new high in March 2005, the Consumer Confidence Index (CCI) slipped 2.1 points over Q2'05, to 105.2. The CCI value has now been above the 100-mark since March 2004, which shows that a positive mood prevails in Ukrainian society. After a steep improvement in economic expectations at the beginning of the year, the Index of Economic Expectations (IEE) dropped 8.6 points over Q2'05, to 108.4. Despite this decline, the IEE remains higher than the values registered over the entire period since consumer confidence research began in Ukraine, that is, from late 2000 through late 2004. The decline in this index over Q2'05 appears to be an adjustment of the extremely high expectations among consumers during the post-election period registered in the March 2005 survey.

Indices

Consumer Confidence Index (CCI)	105.2 -2.1
Index of the Current Situation (ICS)	100.5 +7.6
Index of Economic Expectations (IEE)	108.4 -8.6
Index of Expected Changes in Unemployment (IECU)	111.0 +12.1
Index of Inflationary Expectations (IIE)	182.2 +0.2
Index of Current Personal Financial Standing (x1)	94.6 +1.3
Index of Expected Changes in Personal Financial Standing (x2)	102.7 -6.6
Index of Expected Economic Conditions in the Country Over the Next Year (x3)	110.8 -11.2
Index of Expected Economic Conditions in the Country Over the Next 5 Years (x4)	111.7 -8.0
Index of Propensity to Consume (x5)	106.3 +13.9

Sources: GfK-USM, ICPS

Despite deteriorating economic expectations, the current financial standing of Ukrainians improved over Q2'05: the Index of the Current Situation (ICS) grew 7.6 points over March 2005, to 100.5. The ICS improved mainly because the Index of Propensity to Consume (x5) grew: over the quarter, this index rose 13.9 points to reach a new record high of 106.3. The Index of Propensity to Consume shows the readiness of Ukrainians to make large household purchases. The propensity to consume appears to be driven by high inflationary expectations among consumers.

In June 2005, the Index of Inflationary Expectations (IIE) stood at 182.2. Over the last four quarters, the IIE has remained high, its value fluctuating in the 180–182.5 range. However, another factor behind the growing propensity to consume is the growth in household incomes. Over January–May 2005, real disposable incomes jumped 26.2%, compared to the same period in 2004.

Western Ukraine continues to show the most optimistic expectations: its CCI rose 3.8 points over the quarter, to 122. An improvement in consumer confidence was also registered in eastern Ukraine. Over Q2'05, this CCI inched up 1.6 points. The main factor behind improved consumer confidence in this region was a significant growth in the propensity to consume: this index soared 22.4 points over Q2, to 109.1. This value for eastern Ukraine is slightly lower than the record registered in March 2004, 110.6.

The propensity to consume grew the most among residents of large cities,

New issue of Local Governance Brief

As Europe seeks to tackle the challenge of regional development of the newly enlarged EU, the countries of Central and Eastern Europe are in line for massive investments through the Structural Funds and pre-accession instruments. While cohesion policy is widely acknowledged as useful by the least advanced regions, experts are divided on how effective the Structural Funds really are. The new issue of the Russian-language issue of Local Governance Brief published by ICPS in August highlights important debates surrounding these policy proposals, and to encourage further debate and discussion on the matter.

The feature section discusses the Commission's proposals in light of the Lisbon Agenda for making the EU more competitive—and in light of upcoming negotiations about the future EU budget. The features also highlight two controversial reports that recommended drastic changes in cohesion policy and examine regional lobbying in Brussels. The case study section will present a number of cases illustrating the art and craft of managing Structural Funds. Most of the cases stress the importance of having the right approach, with good strategies, strong partnerships, and capable institutions.

During the 2004–2006 period, the EC is working on a program to better coordinate the various programs that have been used to send aid to countries outside the EU. Much of the aid will be cross-border funding, which will go to pay for development in regions that include the countries of Central and Eastern Europe and their neighbors across the border.

The Russian-language Local Governance Brief magazine is quarterly published by the LGI program of the Open Society Institute, Budapest, Hungary. ICPS translates Local Governance Brief into Russian and distributes it gratis. You can subscribe to the Russian-language version online at: http://www.icps.kiev.ua/subscribe/.

where this index skyrocketed 41.8 points over the quarter, to a record-high 134.8. The CCI in large cities also reached a new record of 118.4, 18.5 points above the level registered in March 2005 and 5.9 points above the previous record, in June 2004.

Since the beginning of the year, optimistic economic expectations have dominated among Ukrainians with below-average incomes. In June 2005, the IEE stood at 103.4. Over Q2, the Index of Propensity to Consume for this income group grew the most among all income groups, leaping 17.7 points to 93.1. The latest poll also shows that low-income Ukrainians have the highest inflationary expectations: their IIE hit 185.5 in June 2005. ■

You can read in greater detail about the mood of Ukrainian consumers in "Consumer Confidence," a quarterly report published by ICPS jointly with GfK–USM—one of the leading companies that survey the Ukrainian market. If you would like to subscribe to the Consumer Confidence report, contact our client relations and marketing manager Andriy Starynskiy by phone at (380-44) 484-4410 or via e-mail at marketing@icps.kiev.ua. You can also order ICPS publications through the ICPS website, at http://www.icps.com.ua/eng/subscribe/. For further information on the Ukrainian consumer confidence survey, contact Yevhenia Akhtyrko at (380 44) 484-4403 or via e-mail at eakhtyrko@icps.kiev.ua.

The aviation sector: Leader or outsider—everything depends on state policy

Ukraine has a good deal of latent transit potential in the aviation branch, which could bring profits at the same scale as the profits from transporting gas. Different options for the strategic development of this branch and ways of eliminating some of the current problems were discussed on 28 July 2005 by representatives of the government, airlines, and aviation infrastructure companies, and experts at a roundtable called "Which strategy should Ukraine follow for air transport in the 'open skies' context?"

Ukraine's transit potential remains completely untapped

The air passenger market is one of the fastest growing in Ukraine today. The development of both regional and international transport has been strongly influenced by the growth of the country's economy and the expansion of transit traffic during the last five years.

Ukraine can continue to significantly increase its volumes of both passenger and cargo air traffic. Firstly, the country is conveniently located and has several international airports, particularly Boryspil International Airport, which would allow Ukraine to attract serious transit traffic. Even if air transport has only a small share of the country's overall transport sector today, the potential for air transit is comparable to the potential of its transit pipeline networks. Secondly, the long tradition of a developed aviation industry and air transport ensures the presence of a qualified professional work force and the necessary technical and professional educational facilities.

Domestic airlines are not ready for prime-time

Today, not a single Ukrainian airline is capable of competing on a level field with the top international airlines if the market is liberalized. The experience of Central European countries, who liberalized their domestic air transport markets upon entering the EU, showed that mid-sized domestic carriers cannot hold their own in competing with the European majors and, as a rule go bankrupt, drop their international destinations, especially long haul ones, or give up and merge with their competitors.

The state must initiate and carry out the restructuring of both this branch and its companies in order for the market to develop any further, since the presence of major international airlines or portfolio investors could conflict or be incompatible with the interests of Ukrainian society.

If the current situation, with its lack of clarity as to further state policy in this branch, continues, it will have negative long-term consequences for Ukraine. The opacity of state policy will get in the way of the strategic plans of market participants, while the inability of domestic carriers to defend their interests during international negotiations will cut into their revenues, and therefore into Budget tax revenues. Ukraine could lose its advantages as an air transit country, while the domination of international carriers will complicate national security in civil aviation.

The top airlines need to join forces

There are four options for using the country's transit potential in the aviation branch:

- Maintaining status quo;
- Establishing a state carrier;
- Establishing an international network carrier based on one of the market leaders;
- Merging the two top companies in terms of international routes, AeroSvit and UIA.

The option of consolidating the two top airlines could be the best one, given that it will allow the popular flying destinations of the two companies to be combined into a single well-balanced network. Establishing an alliance specifically on international routes also makes it possible to avoid diminishing competition on the domestic market as a result of a merger. ■

For the full analytical report, which was based on the results of discussions with stakeholders at a roundtable and other materials, visit the ICPS website at: http://www.icps.kiev.ua/project.html?pid=90. Hard copies of this report are available in Ukrainian, English and Russian through ICPS. To get your copy or for any other questions regarding the aviation industry in Ukraine, contact Ildar Gazizullin at (044) 484-4400 or by e-mail at igazizullin@icps.kiev.ua.

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To be included in the distribution list, mail your request to: marketing@icps.kiev.ua.
icps newsletter editor: Yevhen Shulha (shulha@icps.kiev.ua)
Phone: (380-44) 484-4400. Fax: (380-44) 484-4402.
English text editor: L.A. Wolanskyj

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Address: vul. Pymonenka 13A, Kyiv, Ukraine 04050
Web-site: *http://www.icps.com.ua/eng/*