

# consumer confidence®

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## Consumer confidence: number of optimists reaches record high

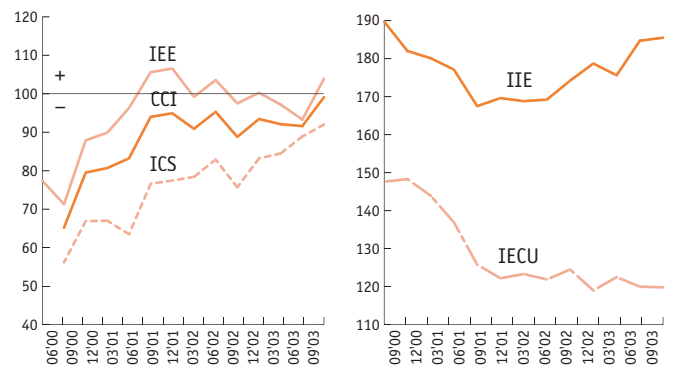
*In Ukraine, the Consumer Confidence Index (CCI) reached 99.1 points (with a possible range of 0 to 200) in September—the highest level since the commencement of regular surveys in September 2000. Overall, the CCI increased by 34 points during the three years of research; the previous record of June 2003 was exceeded by 7.6 points. Consumer confidence improved for the first time this year. Inflationary expectations of consumers remain high. In this issue, we present an analysis of data on consumer confidence in Ukraine during the last three years, and the results of an extensive survey conducted in October 2003*

### Optimism grows despite inflationary expectations

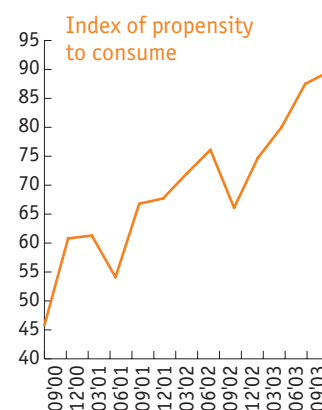
During Q3'03, the CCI resumed its upward trend for the first time since December 2002 and reached a new record high of 99.1 points in September, which was 7.6 points higher than the previous record, observed in June 2003. The improvement of consumer confidence was primarily due to more optimistic expectations of individuals regarding the development of the economy.

Following two consecutive quarters of decline, the Index of Economic Expectations increased during the quarter by 10.5 points to 103.9. Currently, Ukrainians have predominantly optimistic expectations regarding the development of the

Index of current personal financial position (x1)	94.4	+4.1
Index of expected changes in personal financial position (x2)	105.7	+4.6
Index of expected economic conditions in the country within the nearest year (x3)	103.6	+22.3
Index of expected economic conditions in the country within the nearest 5 years (x4)	102.3	+4.7
Index of propensity to consume (x5)	89.6	+2.1
<b>Consumer Confidence Index (CCI)</b>	<b>99.1</b>	<b>+7.6</b>
Index of the Current Situation (ICS)	92.0	+3.1
Index of Economic Expectations (IEE)	103.9	+10.5
Index of Expected Changes in Unemployment (IECU)	119.8	-0.2
Index of Inflationary Expectations (IIE)	185.5	+0.8



domestic economy, both in the short run and the long run. The Index of Current Situation also reached a new record high of 92.0, and exceeded the previous indicator by 3.1 points.



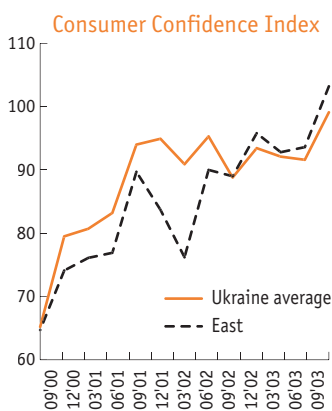
At the same time, the inflationary expectations of Ukrainian consumers remain very high; in September, the Index of Inflationary Expectations totalled 185.5 points, the highest level recorded since December 2000. Expectations regarding unemployment remain at a relatively low level (119.8); the respective index during Q3'03 did not undergo statistically significant changes.

### Optimism prevails in the East, in large and small-sized cities

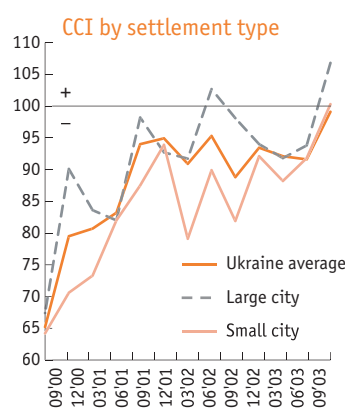
Consumer confidence advanced in all regions of Ukraine. The highest CCIs were observed in Kyiv and the Eastern Region. In the east of the country, the index totalled 103.2 points, exceeding the results of the previous quarter by 9.6 points. This index exceeding the 100-point benchmark was observed for the first time in this region; such a record indicates that the majority of individuals who reside in Eastern oblasts currently have positive consumer confidence. The Index of Economic Expectations in this region also reached a record high of 105.9 by gaining 15.1 points during the quarter. The substantial improvement of consumer confidence in the Eastern Region is related to accelerated industrial growth in the country.

Index	Kyiv	North	West	Centre	South	East
1	100.0 -8.9	86.1 -2.6	93.1 +3.7	88.2 +10.1	89.7 +6.4	101.5 +5.6
x2	126.8 +23.2	110.4 +3.5	102.8 +4.1	100.0 +0.8	104.5 +4.5	105.0 +3.6
x3	114.3 +28.6	93.0 +10.4	100.5 +19.8	99.2 +31.1	103.8 +12.2	108.6 +28.2
x4	110.7 -10.7	100.0 +6.1	101.8 +2.8	93.3 -10.1	104.5 +3.8	104.2 +13.6
x5	139.3 -7.1	72.2 +11.3	84.8 +24.0	76.5 -5.9	85.9 -14.7	96.7 -3.3
<b>CCI</b>	<b>118.2</b> <b>+5.0</b>	<b>92.3</b> <b>+5.7</b>	<b>96.6</b> <b>+10.9</b>	<b>91.4</b> <b>+5.2</b>	<b>97.7</b> <b>+2.4</b>	<b>103.2</b> <b>+9.6</b>
ICS	119.6 -8.0	79.1 +4.3	88.9 +13.8	82.4 +2.1	87.8 -4.2	99.1 +1.2
IEE	117.3 +13.7	101.2 +6.7	101.7 +8.9	97.5 +7.3	104.3 +6.8	105.9 +15.1
IECU	117.9 +17.9	146.1 +7.8	106.5 -13.4	114.3 -14.3	117.3 +9.6	123.1 +3.3
IIE	196.4 +26.8	189.6 +2.6	183.4 +5.5	183.2 -5.9	184.6 -6.4	184.6 -1.8

Index	Village	Town	Small city	Large city
x1	91.3 +4.5	90.9 +0.6	95.8 +6.3	103.2 +12.1
x2	99.3 +2.4	104.2 -1.9	105.8 +6.8	112.7 +12.1
x3	99.0 +22.1	108.1 +20.8	97.4 +15.3	107.0 +31.8
x4	97.9 +5.2	104.2 +2.6	106.3 +11.1	98.7 +5.7
x5	74.4 +2.8	79.2 +1.6	96.3 +3.2	112.1 +3.2
<b>CCI</b>	<b>92.4</b> <b>+7.4</b>	<b>97.3</b> <b>+4.7</b>	<b>100.3</b> <b>+8.5</b>	<b>106.8</b> <b>+13.0</b>
ICS	82.9 +3.6	85.1 +1.1	96.1 +4.7	107.6 +7.6
IEE	98.7 +9.9	105.5 +7.1	103.2 +11.1	106.2 +16.6
IECU	118.0 -1.7	122.1 -0.3	117.4 -1.1	122.9 -1.9
IIE	184.8 +1.0	186.0 -3.2	187.9 +4.2	179.0 -5.1

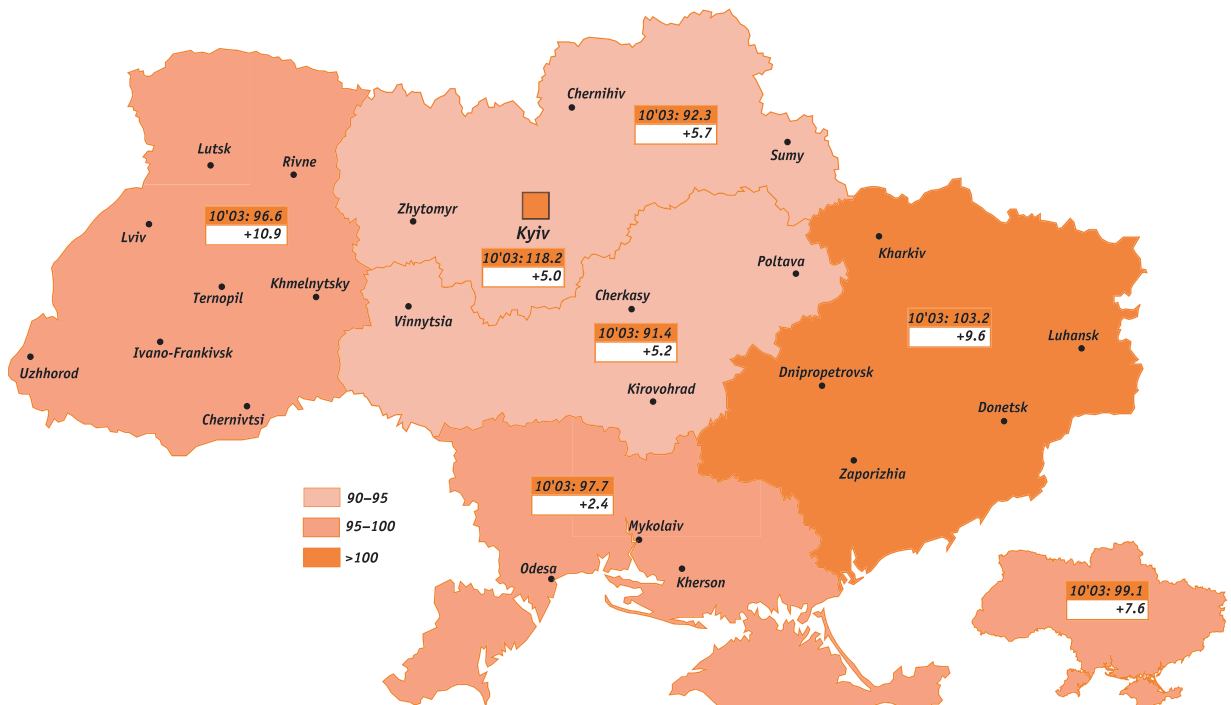


Improvement of the financial situation and growth of optimistic expectations among the residents of Eastern oblasts resulted in a substantial increase in their propensity to consume. During the last 12 months the Index of Propensity to Consume in the Eastern Region exceeded the Ukraine average. Compared to September 2002, the Index of Propensity to Consume in the Eastern

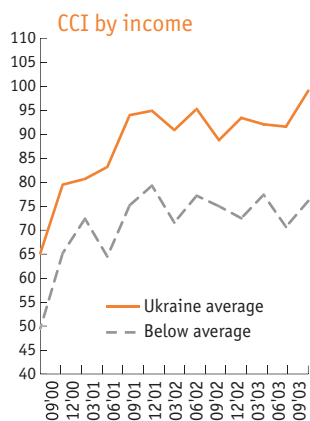


Region increased by 28.2 points, to 96.7. The survey registered the improvement of confidence in all types of settlements. However, the positive consequences of acceleration in overall economic and industrial growth mostly affected the residents of small and large cities, where the CCI in September totalled 100.3 and 106.8 points, respectively.

## Consumer Confidence Index by region

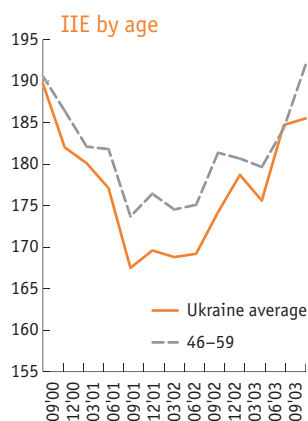


Here we use the following classification of regions: Northern—Zhytomyr, Kyiv (excluding the city of Kyiv), Sumy, Chernihiv oblasts; Southern—Crimea Republic and the city of Sevastopol, Mykolaiv, Odesa, Kherson oblasts; Central—Vinnitsia, Kirovohrad, Poltava, Cherkasy oblasts; Western—Volyn, Transcarpathia, Ivano-Frankivsk, Lviv, Rivne, Ternopil, Khmelnytsky, Chernivtsi oblasts; Eastern—Zaporizhia, Dnipropetrovsk, Donetsk, Luhansk, Kharkiv oblasts.



## Economic growth alone is insufficient for the poor

Confidence improved the most among individuals with above-average income. During the quarter, the CCI of this consumer group increased by 8.1 points, to 122.4. The CCI of individuals with average incomes increased by 5.5 points, to 96.2, and the CCI of those with below-average incomes grew by 5.4 points, to 76.1.



Notably, only the CCI of consumers with below-average incomes did not reach a new record high; the highest confidence of individuals with low income was observed in December 2001, when the corresponding CCI totalled 79.3 points. Evidently, the current acceleration of economic growth has caused an improvement predominantly in the consumer confidence of affluent Ukrainians. To advance the confidence of the least wealthy, special government

Index	Higher-than-average income	Average income	Lower-than-average income
x1	118.4 -4.6	92.8 +4.5	66.1 +3.7
x2	126.4 +3.4	103.7 +3.0	83.3 +3.6
x3	127.2 +32.5	99.1 +16.6	85.0 +21.1
x4	116.0 +1.6	102.5 +5.9	82.8 -0.4
x5	124.0 +7.7	82.8 -2.6	63.3 -1.0
<b>CCI</b>	<b>122.4 +8.1</b>	<b>96.2 +5.5</b>	<b>76.1 +5.4</b>
ICS	121.2 +1.6	87.8 +0.9	64.7 +1.4
IEE	123.2 +12.5	101.8 +8.5	83.7 +8.1
IECU	114.8 +4.3	119.7 +0.3	127.8 -3.9
IIE	185.2 -1.9	185.9 +4.1	185.0 -5.6

Index	15-30	31-45	46-59
x1	105.9 +1.7	95.6 +7.8	76.6 +3.0
x2	117.0 -1.9	104.1 +6.6	91.6 +11.5
x3	115.7 +18.9	102.6 +25.2	87.5 +23.2
x4	110.1 +0.1	102.9 +9.9	90.5 +4.3
x5	102.6 -1.1	89.4 +2.2	71.4 +6.3
<b>CCI</b>	<b>110.3 +3.5</b>	<b>98.9 +10.4</b>	<b>83.5 +9.6</b>
ICS	104.3 +0.3	92.5 +5.0	74.0 +4.6
IEE	114.3 +5.7	103.2 +13.9	89.9 +13.0
IECU	116.0 +2.0	120.3 -0.3	124.9 -2.7
IIE	181.7 +0.1	184.4 -3.9	191.9 +7.7

## How the consumer indexes are calculated

In Ukraine, the CCI is determined through a random survey of the country's population; the survey includes 1,000 people aged from 15 to 59. The people of this age make up 61.3% of the Ukrainian population, and they are the most active consumers. The survey sample is representative by gender and age, and it also accounts for the type and size of settlement. Statistical deviation does not exceed 3.2%.

To define the CCI, the respondents are asked the following questions:

1. How has the financial position of your family changed over the last six months?
2. How do you think your family's financial position will change in the next six months?
3. Speaking of the economic conditions in the country as a whole, do you think the next twelve months will be a good or bad time for the country's economy, or something else?
4. And if we are to speak of the next five years, will they be for the country's economy a good or bad time?
5. Speaking of large purchases for the home, do you think it's generally a good or bad time to make those purchases now?

Using the responses to these questions, the corresponding indexes, listed below, are calculated:

- index of current personal financial position (x1);
- index of expected changes in personal financial position (x2);
- index of expected economic conditions in the country within the nearest year (x3);
- index of expected economic conditions in the country within the nearest 5 years (x4);
- index of propensity to consume (x5).

Indexes are constructed in the following way: from the portion of positive answers the portion of negative answers is deducted, and to this difference 100 is added in order to eliminate the appearance of any negative values. On the basis of these five indexes, three aggregated indices are calculated:

- consumer confidence index (CCI)—arithmetic average (AA) of indexes x1-x5;
- index of current situation (ICS)—AA of indexes x1 and x5;
- index of economic expectations (IEE)—AA of indexes x2, x3, and x4.

Index values range from 0 to 200. The index value equals 200 when all respondents positively assesses the economic situation. The index totals 100 when the shares of positive and negative assessments are equal. Indexes less than 100 indicate the prevalence of negative assessments.

To determine the Index of Expected Changes in Unemployment (IECU) and the Index of Inflationary Expectations (IIE), respondents are asked the following two questions:

1. Do you think that within next 12 months the number of unemployed (people who do not have job and are looking for it) will increase, remain roughly the same, or decrease?
2. Do you think that the prices for major consumer goods and services will change in the next 1-2 months?

The IECU and the IIE are calculated in the following way: from the portion of answers which indicate the growth of unemployment (inflation), the portion of answers which indicate the decrease of unemployment (inflation) is subtracted, and to this difference 100 is added to eliminate the appearance of negative values. The values of indexes can vary within the range of 0 to 200. The index totals 200 when all respondents expect an increase in unemployment (inflation).

measures are definitely required, such as increases in pensions and social assistance.

Confidence improved significantly among individuals of middle age and older. The CCI of middle-aged individuals (31–45 years) increased by 10.4 points, to 98.9, and the confidence of older

citizens (46–59 years) improved by 9.6 points to 83.5. At the same time, the CCI of the younger age group increased less significantly, by 3.5 points, to 110.3. Despite the growing optimism of older people, the inflationary expectations of this age group reached an historic record high, exceeding all previous indicators; during Q3'03, the respective IIE gained 7.7 points and totalled 191.9.

## Reasons for optimism and pessimism: results of the extensive survey

### Ukrainians have begun earning more

As in the previous year, improvement of the financial situation of Ukrainians resulted from increased household income and new or supplementary employment; these reasons for improvement in financial standing during previous six months were cited by 74% of the respondents in October 2003. The second most significant reason for the improvement of material wealth of citizens is the decrease in wage arrears, regular payment of wages and pensions; in October 2003, this reason for improved financial standing was indicated by 17% of respondents while in October 2002 it was cited by 13% of respondents.

Citizens generally attributed a decrease in their financial situation over the past six months to inflation. In October 2003, 60% of respondents who reported decreased material wealth noted that prices increased faster than their income, while in October of 2002, the share of respondents citing this reason was 35%.

### Increased production and investment will spur economic growth

In October 2003, 34% of Ukrainians believed that the next 12 months will be a favourable period for the development of the domestic economy, as production and investment will grow; last year, the proportion of such respondents was 29%. The reason for the increase of such expectations was apparently the acceleration of overall economic and industrial growth. At the same time, the proportion of individuals who believed that the political and economic standing of the country will be firm and that the respectability of the country will increase grew from 18% to 23%, and the proportion of those who expected positive changes in tax legislation and the development of entrepreneurship grew from 14% to 20%.

As in October 2003, the majority of pessimists stated that the next 12 months will be an unfavourable period for development of the economy because the standard of living of citizens will decrease, prices will increase rapidly, and there will be more unemployment; the increase in the proportion of such respondents compared to the previous year (from 51% to 68%) we attribute primarily to increased inflationary expectations.

### Consumer loans help citizens purchase durable goods

During Q3'03, the propensity of individuals to consume continued to grow; the respective index x5 increased during the quarter by

2.1 points and reached a new record high of 89.6. Overall, this index increased by 43.8 points over three years of consumer confidence research in Ukraine. The major causative factor which drives people to make large purchases is a wide selection of goods; in October 2003, this reason was cited by 74% of respondents who believed that now is generally a good time to make large purchases for the home.

Over the preceding 12 months, the proportion of consumers, who believed that large purchases are to be made now because it is possible to get consumer loans and that interest rates on such loans are low. This reason was cited by 52% of optimistic respondents, while in October last year the proportion of such respondents was 29%.<sup>1</sup> Such changes in consumer behaviour of Ukrainians are related to rapid growth in the market for consumer credit.

For the absolute majority of respondents who believed that now is generally a bad time to make large purchases for the home, the major reason for such an opinion was their poor financial situation and low income; in October 2003 this reason was cited by 90% of pessimists.

### Save now, spend later

Over the past 12 months, the propensity of Ukrainians to save increased: the respective index<sup>2</sup> increased from 49.6 to 55.1 points. The major reasons for the greater willingness of people to save were the improvement of their financial standing (42%), that is, the cash income of household was sufficiently large to save, as well as the existence of reliable ways to save (40%). The survey indicated that citizens' current savings behaviour has a "consumption flavour"; 44% of consumers would like to save for large purchases in the future, while only 8% of citizens would like to retain their savings.

The main reason for negative attitudes to saving was the lack of money for savings and the expenditure of all income on current consumption; this reason was cited by 54% of respondents who believed that now is generally a bad time for saving. In October 2002, the proportion of such individuals was 66%.

<sup>1</sup> Respondents could select more than one response.

<sup>2</sup> The Index of Propensity to Save is the "antipode" to the Index of Propensity to Consume. For determining this index, respondents are asked if now is generally a favourable or an unfavourable time to save.



The Consumer Confidence Index is researched jointly by the GfK-USM company and the International Centre for Policy Studies.

GfK-USM is one of the leading Ukrainian market research companies. In 1998, the company joined the worldwide GfK research network, which includes 104 companies in 42 countries.

The International Centre for Policy Studies is an independent research organisation whose goal is to facilitate the improvement of Ukrainian policy research.

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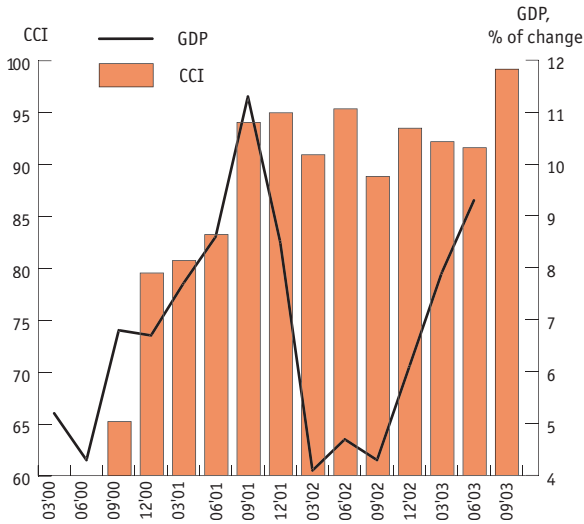
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# Ukrainian consumer behaviour: three year of surveys



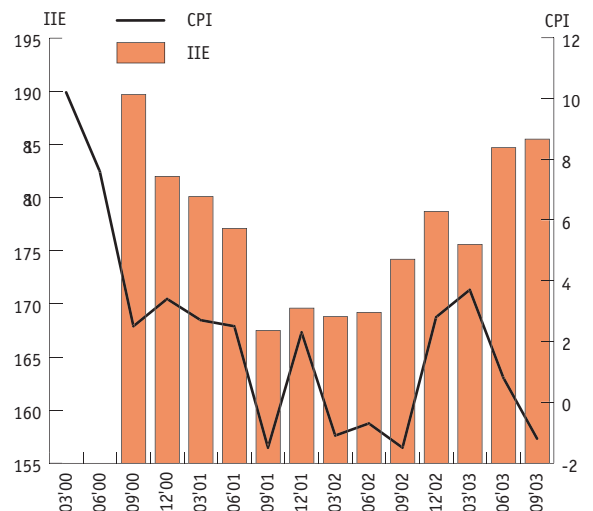
Since the commencement of regular surveys in Ukraine three years ago, in September 2000, the national Consumer Confidence Index has increased by 34 points, the Index of Current Situation has increased by 36 points, and the Index of Economic Expectations has increased by 33 points.

The CCI improved continuously since the beginning of the surveys until the end of 2001; during this period, the index increased by 29.7 points. The CCI then stagnated during 2002 and the first two quarters of 2003, fluctuating around the mean of 92 points. Finally, the index increased sharply during Q3'03 and reached a historic high of 99.1 points.

Although the CCI in Ukraine did not change significantly during 2002 and H1'03, the IEE and ICS underwent substantial changes. In particular, while the CCI continued its upward trend, the IEE during this time experienced generally negative

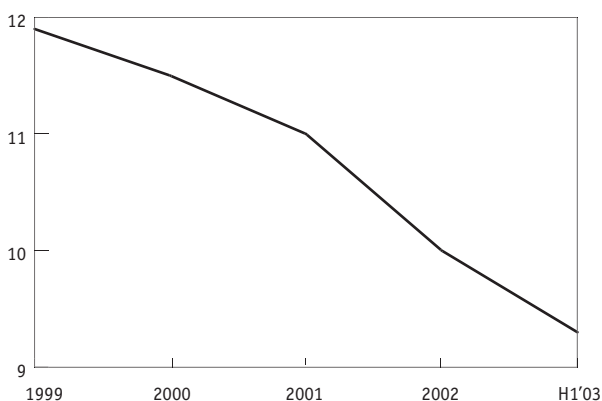
change. This means that during this period, consumers had been reporting improvement in their personal financial standing, while their expectations regarding the development of the domestic economy continued deteriorating overall. Presumably, the long-lasting economic growth in Ukraine resulted in respective increased income, which affected consumer confidence; at the same time, Ukrainians became more demanding as regards the quality of economic growth. Only a high rate of growth can now bring about an increase of positive consumer expectations regarding the development of the economy.

A comparison of GDP and CCI trends in Ukraine shows that during a period of overall economic growth, consumers react somewhat belatedly to changes in the growth rate of the economy. In particular, the steep increase in the GDP growth rate from H2'00 to Q3'01 created among Ukrainians a substantial "reserve" of consumer optimism; as a result, consumers did not react immediately to a steep deceleration of the economic growth rate that took place during the four following quarters, and the slight downward trend of the CCI became evident only in H2'02. Again, Ukrainians reacted belatedly to the acceleration of economic growth that began at the end of 2003; the improvement of consumer confidence became apparent only in Q3'03. However, it should be noted that the consumer confidence at the beginning of this summer was negatively affected by destabilisation in the Ukrainian food market.



As comparison of the consumer price index (CPI) and the CCI shows, Ukrainian consumers are more sensitive to inflation. In particular, inflationary expectations of consumers were in line with the downward trend of inflation from H2'00 to H1'02. In Q3'02, consumers "predicted" the price increase that started at the end of 2002. The high inflationary expectations that were observed in Q2 and Q3'03 indicate a high probability of a new period of inflation at the end of 2003 and at the beginning of 2004.

## Unemployment level, %



Over the three years of consumer confidence research, the Index of Expected Changes in Unemployment dropped by 27.8 points, from 147.6 to 119.8, which shows the significant increase of positive expectations regarding the situation in the labour market. Such expectations of Ukrainians are in line with real trends in the unemployment rate, which according to the methodology of the International Labour Organisation dropped over the past three years by more than 2 p.p.