

ICPS newsletter[®]

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Many obstacles on the road to recovery for Ukraine

ICPS economists have taken a look at trends in economic growth over the next few years. According to their forecasts, GDP will decline 14.5% for 2009. The Consumer Price Index (CPI) will reach 14.0%, while Producer Price Index (PPI) will rise somewhat more, 14.2%. The country faces considerable obstacles to recovery, they write

At the moment, Ukraine's economy is showing a variety of vectors of growth. Over October–November, there were both positive and negative trends. Consumer inflation was lower this fall than in over 2004–2008 as the growth of nominal incomes tapered off. The hryvnia exchange rate has also remained relatively stable, despite the fact that NBU reserves have contracted marginally.

Still, among the bad news is that the IMF has postponed the issuing of its fourth tranche because Ukraine failed to carry out its commitments. Meanwhile, Fitch, a ratings agency, lowered its long-term rating for Ukraine in foreign currency from B to B-.

The ICPS forecast is for GDP to fall 14.5% over 2009, which is marginally worse than the previous forecast. Among others, ICPS economists revised their forecast for industrial output downward.

They are also of the opinion that the hryvnia will weaken once more before the end of 2009 because of growing demand for dollars on the part of importers and private individuals and because of continuing political instability. Still, the NBU policy of extracting hryvnia is working against a weakening and ICPS economists predict this will happen closer to the election. A shortage of hryvnia in circulation led to the relative stability of the exchange rate over September–November, even in the face of bad news, especially

regarding the delayed IMF tranche. To slow down the rise of imports, the hryvnia will gradually be depreciated over 2010.

ICPS economists downgraded their forecast for consumer inflation to 14.0% but raised their forecast for producer prices to 14.2%, based on new data for indicators that affect prices. ICPS analysts do not anticipate any significant increase in rates for gas and other regulated prices affecting households by the end of 2009 and say that the raise in the minimum wage that was recently passed into law will not take effect this year.

During the forecast period, the Budget deficit will be high, as much as 8% of GDP. This year, the Government will be forced to curtail several expenditures because of the lack of resources to cover the deficit. To prevent the deficit from growing over 2010–2012, it will be necessary to take a number of unpopular measures, including raising regulated prices and launching reforms of the social security system (pensions and others). Most likely, the new Government will come to agreement with Russia about postponing the paying off of Naftogaz Ukrainy's debts in exchange for "closer" cooperation in the energy sector.

The risks that consumer inflation will take off in 2010 are growing. After the election, NBU policies will likely become less independent,

Some more interesting reading

- The next issue of *European focus* features the article, "Ukraine and the Energy Community: The law of attraction." http://icps.com.ua/files/articles/54/64/EF_October_2009_UKR.pdf
- The first issue of *socio-economic focus* has been published under the Social Economy Program. http://icps.com.ua/files/articles/54/67/SEF_October_2009_UKR.pdf

one consequence of which might be increased emissions of hryvnia to finance the Budget deficit. This could accelerate the growth of nominal wages and consumer prices.

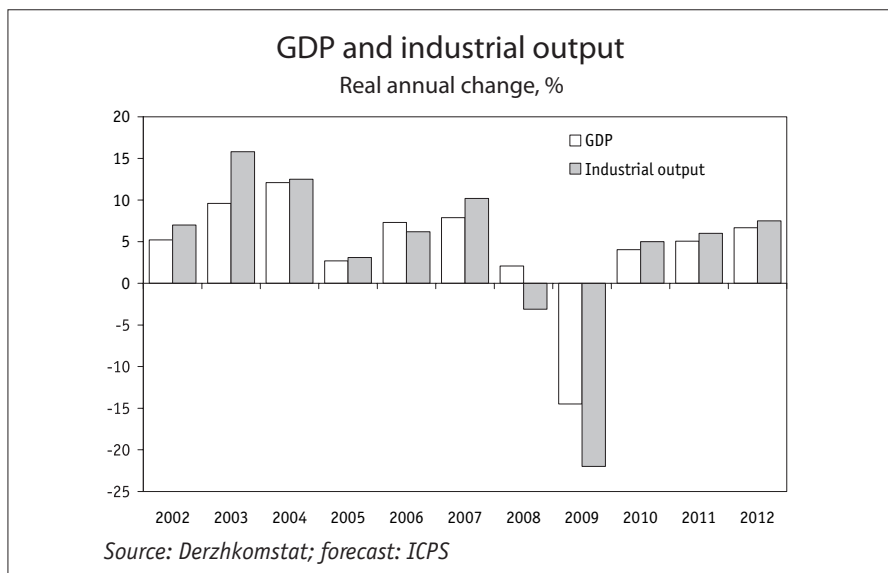
ICPS analysts upgraded their forecast for economic growth over 2010–2010 to 4%, 5% and 7%. The main factor behind this growth will be an improved outlook for the world economy. The risks to these forecasts are the usual ones and are mainly related to outside shocks that could damage the Ukrainian economy because of its considerable openness:

- insufficient inflows of capital to cover payments related to external debts over 2009–2011;
- lower-than-expected growth in commodity prices on key export goods: ferrous metals and chemical products;
- faster- or stronger-than-expected growth in prices on import commodities (gas and oil).

The main internal risk is a populist trend towards more public spending that will have to be financed by printing more hryvnias. ■

The ICPS team does economic research on commission from its clients. Right now, subscriptions for **economic insight** for 2010 are being accepted. **Economic insight** is a more flexible, upgraded version of the **quarterly predictions** ICPS has been publishing for over 10 years that includes rolling three-year macroeconomic forecasts, a base of statistical data, and analyses of driving factors and risks.

ICPS is also in the process of launching a new publication called **regional trends**. This periodical will include a base of data regarding the economic potential of Ukraine's oblasts and forecasts. The terms of subscriptions will be formalized shortly.



If you are interested in receiving ICPS periodicals, you can contact Anna Karnaukh by phone at

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Second Media Breakfast

Is it possible to be intellectually stimulated at breakfast? ICPS continues to prove that it is!

On 19 November, some of Ukraine's top journalists were able to experience this during our second Media Breakfast. The topic of this Breakfast, organized by ICPS with the support of the Friedrich Nauman Foundation, was the opportunities and prospects offered by setting up a Free Trade Area between Ukraine and the EU. Journalists were able to talk directly to Olena Zerkal, director of the Department for the Adaptation of Legislation under the Ministry of Justice of Ukraine, her first deputy Taras Kachka, and ICPS senior analyst Ildar Gazizullin.

Since last year, Ukraine has been negotiating an Agreement on an FTA with the European Union, making this topic very current. These talks are focusing, not just on tariffs on goods being traded, but on bringing the regulatory environment in Ukraine in line with EU norms and rules in more than 20 areas. This Agreement could become the engine for internal reform and a real rapprochement between Ukraine and the EU.

Still, as agreed between Kyiv and Brussels, these negotiations are going on behind closed doors, which is standard practice. Nevertheless, it is important that Ukraine's press understand the process and have reliable information at their disposal. For this reason, our guest speakers, who are members of the Ukrainian side of the negotiating team, discussed the opportunities presented by the FTA+ for various stakeholders and problematic issues in the negotiating process, without uncovering confidential information, and discussed probable deadlines for the talks to be concluded.

Media Breakfasts are an ICPS initiative to provide a platform for media professionals and analysts to exchange opinions and ideas on European integration. These Breakfasts take place twice a month and focus on one of five topics: democratization and proper governance; social economy; energy; negotiations on the Association Agreement between Ukraine and the EU; and foreign policy. These events will offer journalists a venue where they can gain exclusive information from Ukrainian and foreign experts on various aspects of Ukraine's integration into the EU and to start the day in stimulating company.

If you would like to be invited to future Media Breakfasts, contact Anna Karnaukh, ICPS Public Events Manager, by phone at (+38-044) 484-4410 or via e-mail at anna.karnaukh@icps.kiev.ua.

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The International Centre for Policy Studies (ICPS) is a leading independent think-tank in Ukraine. ICPS was established at the initiative of the Open Society Institute in 1994. ICPS's mission is to assist the further democratization and modernization of Ukraine through assertive and deliberate Europeanization.

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