

Latest developments in Ukraine

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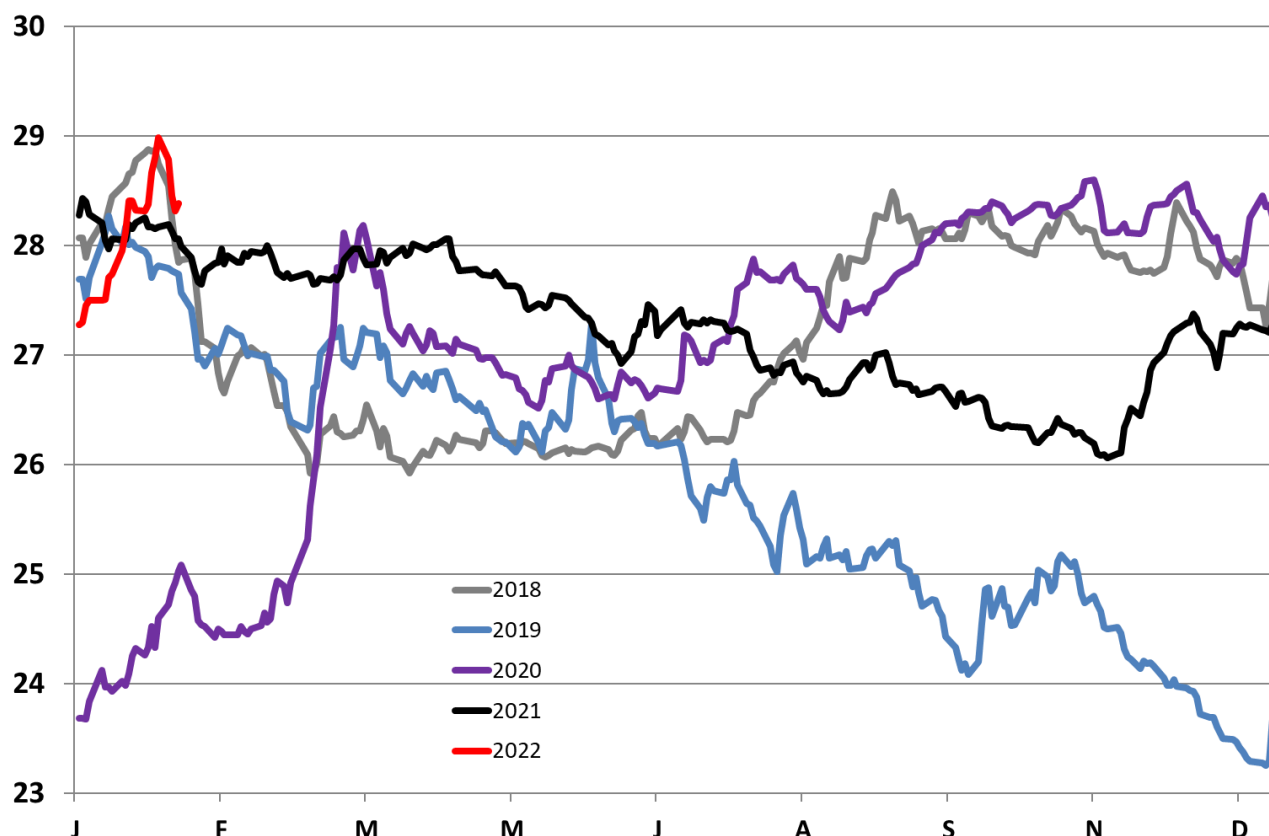


Last week, the Ukrainian FX market was trading in a wide USD/UAH 28.20-29.09 range, with the hryvnia losing another 1.35% to the US dollar over the week. The NBU sold USD 759.5 mln that week.

In January, the Ukrainian currency retreated 3.9% vs. the greenback and 2.7% vs. the euro. NBU sold a net of USD 1.4 bln last month. While the hryvnia is now almost 2% weaker in YoY terms, it is worth noting that the average exchange rate for January 2022 is estimated at USD/UAH 28.06, while the average exchange rate for January 2021 was USD/UAH 28.22.

This week, the hryvnia has strengthened back to USD/UAH 28.30 by the end of trading session today. On Monday and Tuesday, the central bank reemerged on the market with a significant bid for foreign currency.

USD/UAH in 2018-2022



Sources: National Bank of Ukraine, Alfa-Bank Ukraine

Current account back in the red in 2021, led there by record-high investment income. According to the National Bank of Ukraine, the economy returned to its usual state of current account deficit in 2021, with the respective bottom line of USD 2.1 bln (1.1% of GDP). While trade deficit remained stable at 1.6% of GDP, the expansion of the deficit was delivered by super-strong USD 19.1 bln payments of investment

income (interest, dividend, etc.) abroad. Even when readjusted for USD 4.2 bln that is estimated to have been reinvested back (inflating net FDI inflow to USD 6 bln), that is still an impressive cash outflow of almost USD 15 bln (7.8% of GDP). Obviously, this sharp increase reflects how much of 2021 windfall profits by Ukraine's exporters eventually ended up abroad. As a strong opposing current, the estimate for wages earned abroad by Ukrainian residents in 2021 also peaked at USD 15 bln.

Balance of payments in 2016-2021, USD bln

	2016	2017	2018	2019	2020	2021
Current account balance (CAB):	-1.9	-3.5	-6.5	-4.1	5.3	-2.1
Trade balance	-6.5	-8.7	-11.4	-12.5	-2.4	-3.0
Income balance	1.0	1.6	1.3	1.9	3.5	-3.8
<i>Wages earned abroad</i>	6.7	9.1	11.5	12.8	11.7	15.0
<i>Interest, dividends sent abroad</i>	-5.9	-7.7	-10.6	-11.4	-8.6	-19.1
Cross-border transfers balance	3.6	3.6	3.7	6.5**	4.1	4.7
Capital stock balance (CSB):	0.1	0.0	0.0	0.0	0.0	0.0
Financing:	2.4	3.1	4.8	2.9	-6.0	0.4
Net FDI	4.0	3.4	4.9	5.2	-0.1	6.0
Net portfolio investment	0.3	1.8	2.1	5.1	-0.8	1.1
Net other investment	-0.6	0.4	0.7	-1.4	-2.8	-3.3
Net IMF financing	1.0	0.1	-0.7	-1.6	1.0	-0.7
Net derivatives (VRI) financing	—	—	—	—	-0.3	-0.2
<i>Financing before FX reserves use</i>	4.8	5.7	6.9	7.3	-3.1	2.9
NBU reserves*	-2.3	-2.7	-2.2	-4.4	-3.0	-2.5
<i>Errors and omissions</i>	-0.6	0.5	1.7	1.2	0.8	1.7
<i>BALANCE of PAYMENTS: CAB + CSB + Financing + Errors and omissions = 0</i>						

* negative values mean increase in FX reserves (actual FX reserves change might differ slightly due to asset re-pricing, most commonly due to FX rates change)

** includes USD 2.9 bln transferred from Gazprom to Naftogaz in December 2019

Note: balances might not add up due to rounding

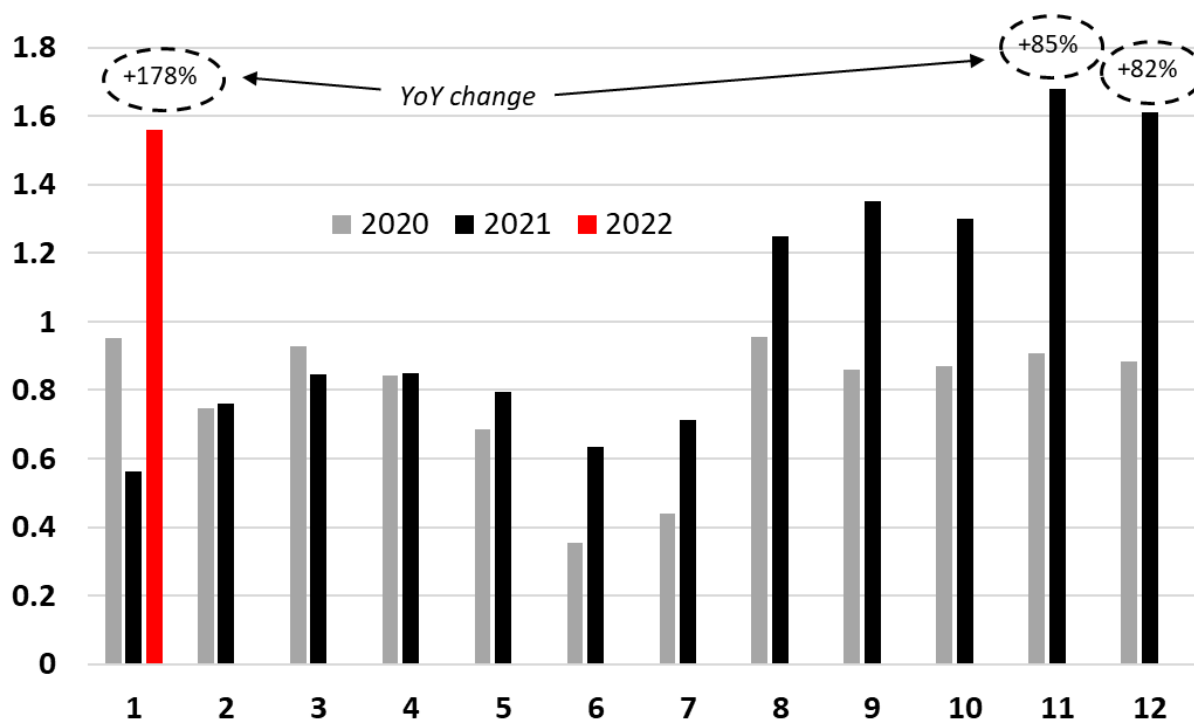
Sources: National Bank of Ukraine, Alfa-Bank Ukraine

It is worth noting that Ukraine still enjoyed a strong primary surplus (CAB+FDI) of USD 3.9 bln (2% of GDP). We expect that to fall back into negative territory of around 1.5% of GDP in 2022.

MinFin buys back another 5.5% VRIs from the market. BoP data confirmed that the Ministry of Finance spent USD 170 mln on buying back GDP-linked value recovery instruments (VRIs, issued as part of the 2015 debt restructuring deal) from the market at the end of 2021. As VRIs traded at 93-95 cents per dollar during the estimated purchase time period, we estimate some 5.5% of VRIs were raised, bringing total MinFin holdings to almost 17% of the total issue. So far, VRIs have not generated meaningful yields as GDP growth has been either close to 3% (2019, 2021) or negative (2020). Recent consensus forecasts center around 3.7% GDP growth in 2022 and 3.5% in 2023, and these seem to us being a little bit on the optimistic side (our forecast is 3.4% and 3%). However, the VRI game should go on till 2038.

Vibrant foreign trade expansion maintained in January. Goods exports amounted to USD 6.03 bln in January, with their growth accelerating to 53% YoY. Due to favorable weather conditions, Ukrainian ports operated almost without interruptions, handling 6 mln tonnes of grain (in January 2021, they managed to haul only less than 3 mln tonnes). Grain export volumes almost tripled in YoY terms, adding an increment of USD 1 bln to total exports compared to January 2021. Overall, food&agriculture exports doubled YoY, accounting for 3/4 of the extra export revenue. Steel exports grew 42% YoY, while iron ore exports were down 33% YoY. However, the latter trend might improve soon, as prices are on the rise again (*see related story further in this report*).

Grain exports by months of 2020-2022, USD mln



Sources: State Customs Service, Alfa-Bank Ukraine

Merchandise imports in January 2022 amounted to USD 7.9 bln, accelerating to 49% YoY. In particular, fertilizer imports more than tripled and coal imports almost tripled, almost solely due to heavy purchase price increases. Imports still have a strong potential to accelerate as Ukraine needs to import a lot of natural gas for the next season as soon as possible (reverse flow capacity is limited and there is a time risk for the next season preparations already), while prices are still very high.

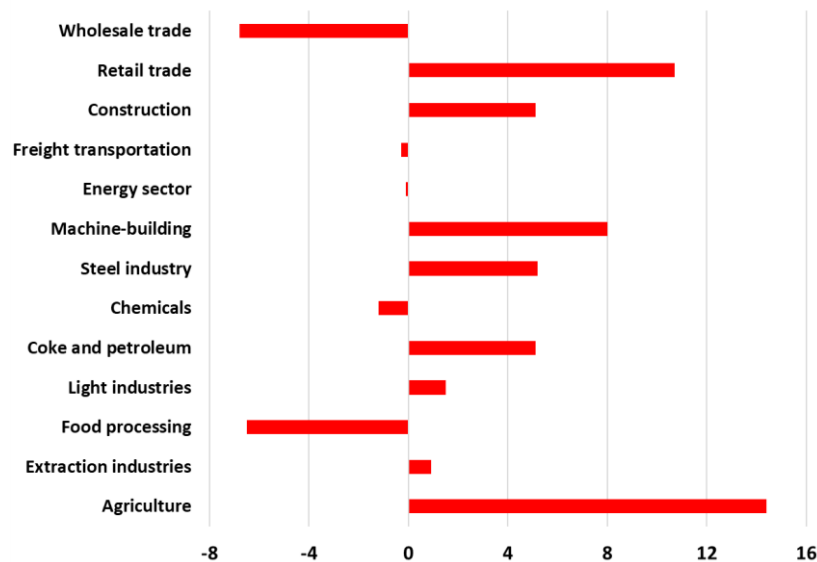
Industrial production back into a decline in December, but still slightly up in 2021.

Industrial output decreased 1% YoY in December. In particular, energy sector output fell 8.3% YoY as weather was mild in the last month of that year. Chemical industry saw its output plunging 18.8% YoY as natural gas prices remained prohibitive for many operations. On the other hand, food processing started to get an upper hand from record-high harvest, restoring growth of 3.3% YoY.

Over 2021, industrial output still increased 1.1%. (This indicator might be upgraded a little bit later, a usual story for Ukrainian industrial statistics.) Construction and

packaging materials and machine-building were the fastest-growing sectors, increasing output 7.5% and 8% respectively (the latter owed mostly to low baseline, while the former demonstrated mostly genuine expansion). As a heritage of a thin “tail” of the 2020 harvest, food processing was the outsider, decreasing output 6.5% in 2021.

Output in key sectors in 2021, % real change

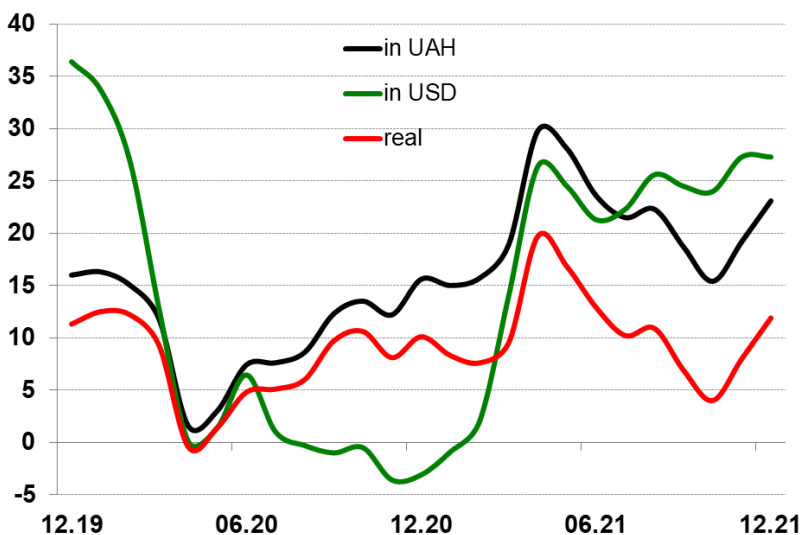


Sources: State Statistics Service, Alfa-Bank Ukraine

Wage growth remains strong. According to the State Statistics Service, average wage in December 2021 amounted to UAH 17,453 (USD 641). That reflects a significant nominal wage growth acceleration from 19.2% to 23.1% YoY, mostly generated by a one-off minimal wage growth acceleration from 20% to 30% YoY.

December is always an outlier as wages are bloated by bonuses. In 2021, average annual wage stood at UAH 14,014 (USD 514). This corresponds to growth of 21% in UAH terms, 20% in USD terms and 10.5% in real terms. The minimum wage effect should wane in 2022 (min. wage just 8.5% up), somewhat cooling off average wage growth.

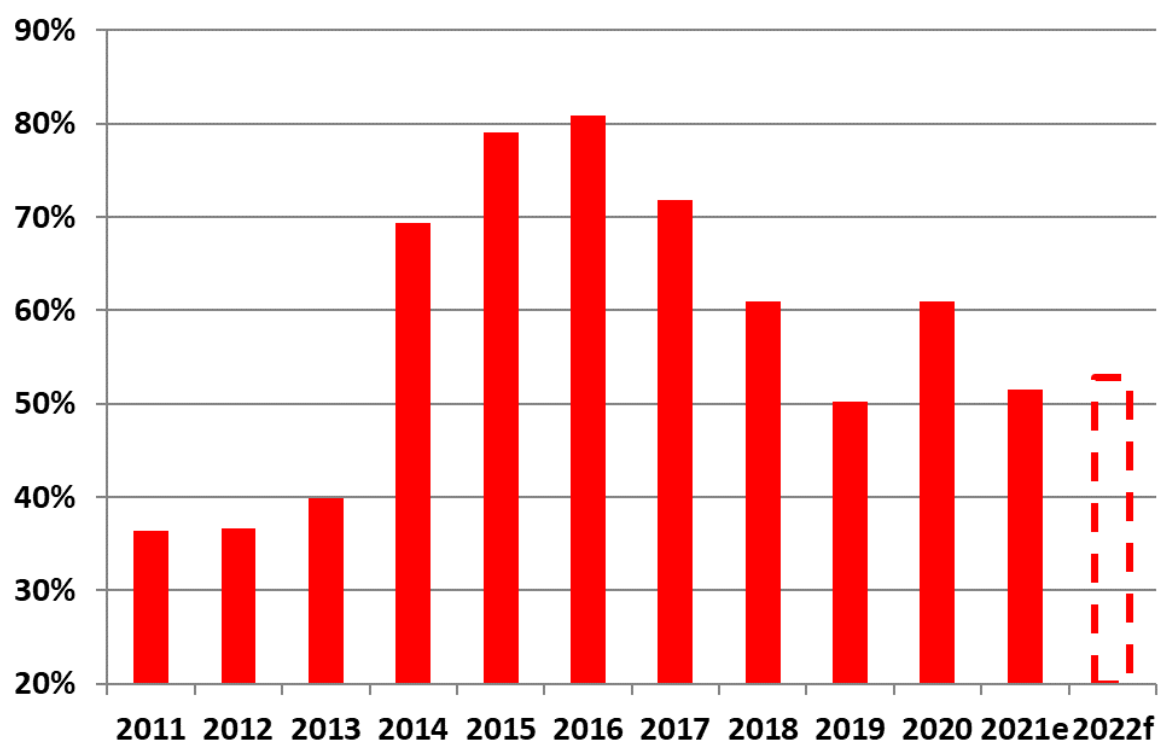
Average wage in 2019-2021, % change YoY



Sources: State Statistics Service, Alfa-Bank Ukraine

Debt-to-GDP ratio down almost 10 p.p. in 2021. In December, public debt increased UAH 113 bln (4.4%). This sharp increase is due to some hryvnia weakening (which always inflates FX part of the debt) and vast financing to cover the gargantuan deficit in December (State Budget deficit in December was UAH 132 bln vs. UAH 66 bln accumulated for the previous 11 months). Actually, total public debt increase over 2021 was almost the same: UAH 120 bln, or 4.7%. According to our estimates, the ratio of public debt to GDP decreased from 60.9% in 2020 to 51.5% in 2021. Most of that decrease owes to inflation that bloated Ukraine’s GDP by an estimated 24% last year.

Public debt (including guaranteed) in 2011-2022, % of GDP



Sources: Ministry of Finance, State Statistics Service, Alfa-Bank Ukraine

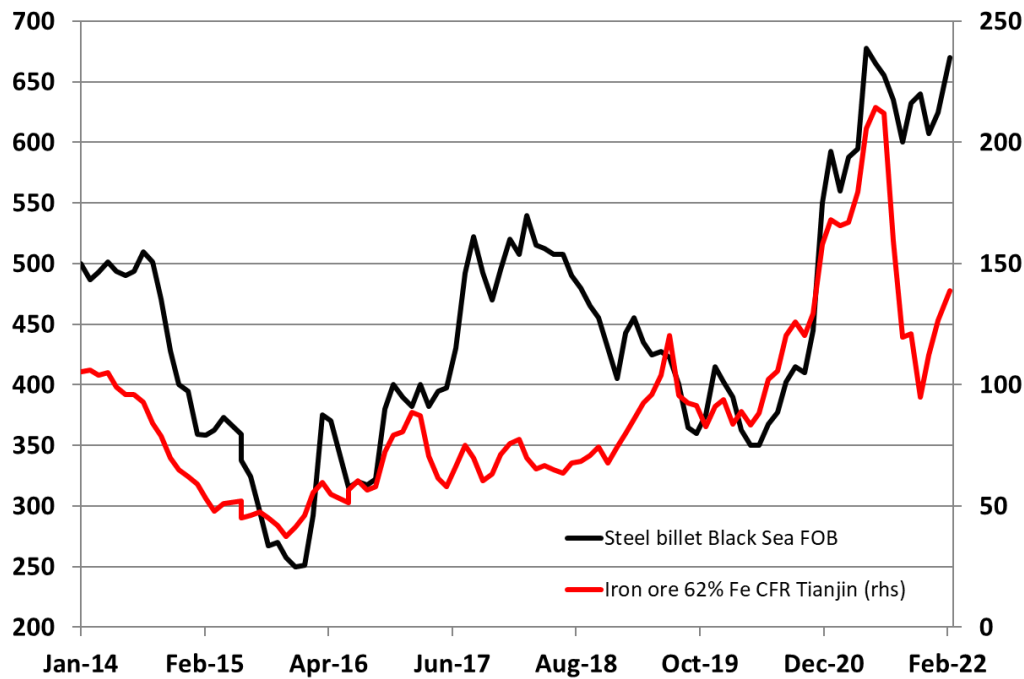
Strong fiscal overperformance over already-outdated State Budget plan. In January, State Budget revenue amounted to UAH 89.1 bln, up 35% YoY. This largely reflects the same inflationary effects which allowed increasing State Budget expenditure vs. original plan by UAH 170 bln (13%) in 2021. The State Budget for 2022 in its current state is poised for similar deviation from the current law. Its revenue plan is just 1.9% above the actual result for 2021, while expenditure plan assumes even less growth, at 0.5%.

If no changes are made in the expenditure plan, Ukraine might well see a fiscal surplus in 2022 instead of the 3.5% of GDP deficit announced originally. However, we expect over UAH 200 bln in extra expenditure to be approved in the course of the year to utilize this ongoing inflationary “fiscal miracle.” Energy and loan subsidies, wages and pensions, cash handouts, and of course the preferred way of road construction: there are plenty of already considered options to fill that expenditure increase.

Ore & steel sector back on the up. According to a flash estimate by UkrMetalurgProm, total average daily steel output rebounded to 59,900 tonnes (increase of 6% MoM and 1% YoY).

Recent weeks have provided significant price increases for the sector. Prices for semis are now near their mid-2021 local peak, while iron ore price has reclaimed more than 20% since the start of 2022 (*the commodity price table at the end of this report has not yet captured strong price increases at the start of this week*).

Iron ore and steel prices in 2014-2022, USD/t



Sources: UkrPromZovnishExpertisa, Market Index, Alfa-Bank Ukraine

Economy-related legislation voted in Verkhovna Rada over the week

Draft Law No.	Content	Status
4278	Increases untaxed value threshold for international parcel shipments back from EUR 100 to EUR 150	Approved
4279	Simplifies customs clearance of international parcel shipments	Approved
5705	On e-tickets in public transit	1st reading passed
6070-1	On technical control over agricultural vehicles	1st reading passed
6133	Allows to divide underground gas storages and gas pipelines into critical and non-critical with option to shut down the latter	1st reading passed
6199	Enhances legislation on land ownership	1st reading passed
6273	Special public procurement rules for certain infrastructure projects for gas transit network and Dniester Hydroelectric Pumped-Storage Power Plant	Approved
6287	Support for book retailers (rent subsidies for stores, provision of book purchase vouchers to Ukrainian citizens)	1st reading passed

Sources: Verkhovna Rada, Alfa-Bank Ukraine

Recent sovereign debt operations and upcoming payments schedule

	New debt	Payments	
		Amortization	Interest
25 January	UAH 2,927 mln	—	—
26 January	—	—	UAH 642 mln
27 January	—	—	EUR 54.7 mln
01 February	UAH 85.8 mln + USD 4.6 mln	—	USD 33.7 mln
02 February	—	UAH 11,504 mln	UAH 1,980 mln
03 February	—	USD 368 mln	USD 13 mln
04 February	—	SDR 98.5 mln*	SDR 43.2 mln
08 February	<i>placement:</i> UAH 3M, 12M, 18M, 2Y, 3Y, 5Y USD 2Y	—	—
09 February	—	—	UAH 448 mln
15 February	<i>placement:</i> UAH 6M, 12M, 18M, 2Y, 3Y, 4Y	—	—
16 February	—	—	UAH 926 mln
17 February	—	EUR 349 mln	EUR 4.4 mln

* paid to the IMF by the NBU (repayment of EFF 2015)

Sources: Ministry of Finance, IMF, Alfa-Bank Ukraine

Prices for key commodities, % change

	over the week	YtD	YoY
Steel	2	7	16
Iron ore	1	16	-22
Corn	2	2	4
Wheat	0	-1	9
Sunflower oil	1	4	8
Crude oil	4	17	62
Thermal coal	3	21	146
Natural gas	12	14	315
Bottom line: change in terms of trade	NEGATIVE	NEGATIVE	NEGATIVE

Sources: Bloomberg, APK-Inform, UkrPromZovnishExpertiza, Alfa-Bank Ukraine

Note: prices as of the start of this week, over the past days there have been strong changes into the POSITIVE side

Ukraine: key macroeconomic indicators

	2019	2020	2021e	2022f
GDP, UAH bln	3,977	4,192	5,185	5,807
GDP, USD bln	155.0	154.7	190.0	205.6
GDP, % real change	3.2	-4.0	3.0	3.4
Industrial output, % real change	-0.5	-4.5	1.1	2.5
CPI, % average annual change	7.9	2.7	9.4	8.4
CPI, % change Dec/Dec	4.1	5.0	10.0	7.5
Average wage, USD	406	430	514	565
Average wage, % real change	9.8	7.4	10.5	5.3
Consolidated Budget balance, % of GDP	-2.1	-5.4	-3.6	-3.5
Public debt (incl. guarantees), % of GDP	50.2	60.9	51.5	52.8
Net FDI inflow, USD bln	5.2	-0.1	6.0	4.0
Current account balance, % of GDP	-2.7	3.4	-1.1	-3.5
FX reserves, USD bln at year-end	25.3	29.1	30.9	29.0
USD/UAH rate, annual average	25.85	26.96	27.29	28.25
NBU key policy rate, % (annual average)	17.0	7.9	7.5	9.6

Sources: State Statistics Service, National Bank of Ukraine, Ministry of Finance, forecast by Alfa-Bank Ukraine

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