

Issue 14 | June 2021

Overview

- Quick recovery: GDP growth of 4.3% in 2021 mainly driven by domestic demand.
- Moderate pre-crisis growth rates around 3.5% expected for next years. Increasing reform ambition is necessary.
- Inflation currently at 9.5%, way above target range (4-6%). NBU has started hiking policy rate to reduce inflation.
- Expansionary fiscal policy continued during recovery. Consolidation and IMF-programme remain important.
- Recovery of external trade driven by favourable terms of trade. ICT now leading service exports.
- Current account surplus remains in 2021. Stable exchange rate and reserves.

Topics

- **IMF programme.** IMF-support remains vital. Reinforced reform effort is necessary.
- **Export finance.** Many obstacles reported by enterprises in a survey. Efficient and strong ECA is needed.
- **ACAA with EU.** Positive direct and indirect effects expected. Institutional alignment is the main challenge.
- **Labour market.** Ability to recover from crises would benefit from extending short-time work scheme.
- **COVID-19.** 7-day incidence is declining. Long way to go before mass vaccination.

Basic indicators

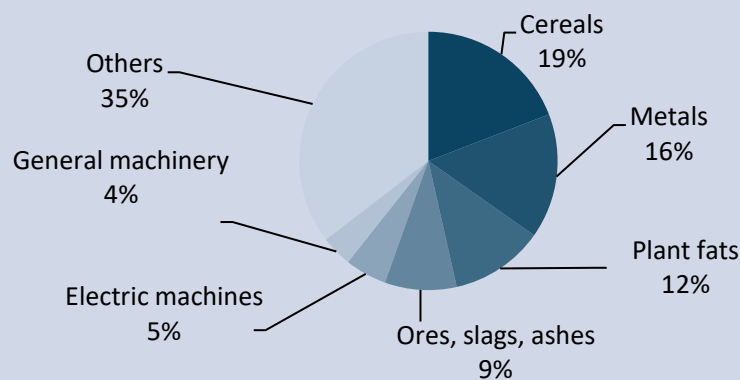
	Belarus	Russia	Ukraine	Moldova	Georgia
GDP, USD bn	60.3	1,473.6	155.2	11.9	15.9
GDP/capita, USD	6,447	10,037	3,709	4,582	4,278
Population, m	9.3	146.8	41.6	2.6	3.7

Sources: National statistics, IMF, 2020

Trade structure

Exports

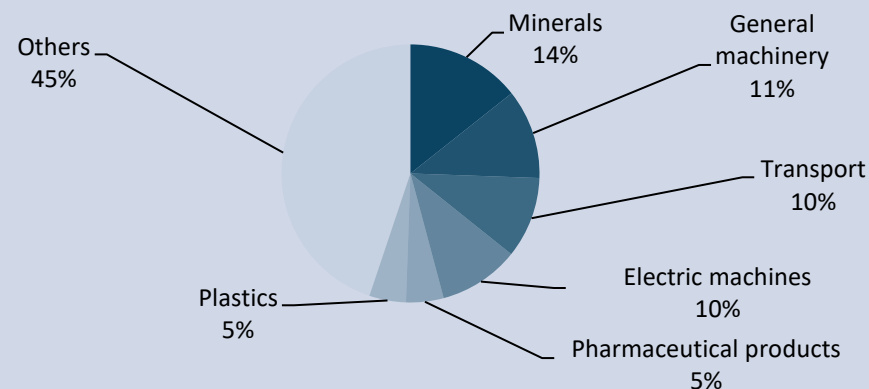
EU 37% | China 14% | Others 49%



Source: Ukrstat, 2020; note: trade in goods

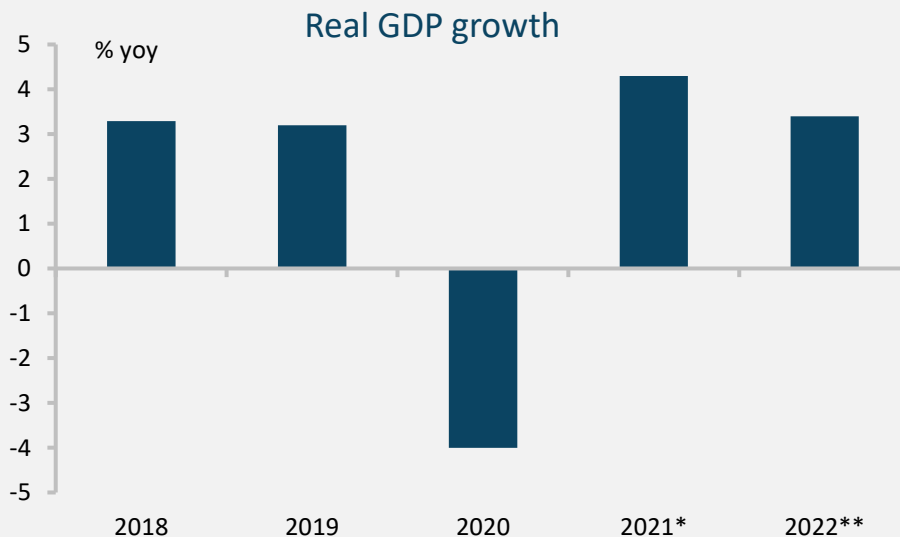
Imports

EU 42% | China 15% | Others 43%



Source: Ukrstat, 2020; note: trade in goods

Economic growth



Sources: Ukrstat, GET/IER, IMF, *GET/IER forecast, **IMF forecast

Regional comparison of real GDP growth, % yoy

	2020	2021	2022
Ukraine	-4.0	4.3	3.4
Belarus	-0.9	-0.4	0.8
Moldova	-7.0	4.8	4.6
Georgia	-6.2	3.5	5.8
Russia	-3.1	3.8	3.8
EU-27	-6.1	4.2	4.4
Germany	-4.9	3.6	3.4

Sources: National statistics, EU-Commission, GET/IER forecasts, IMF forecasts

GDP

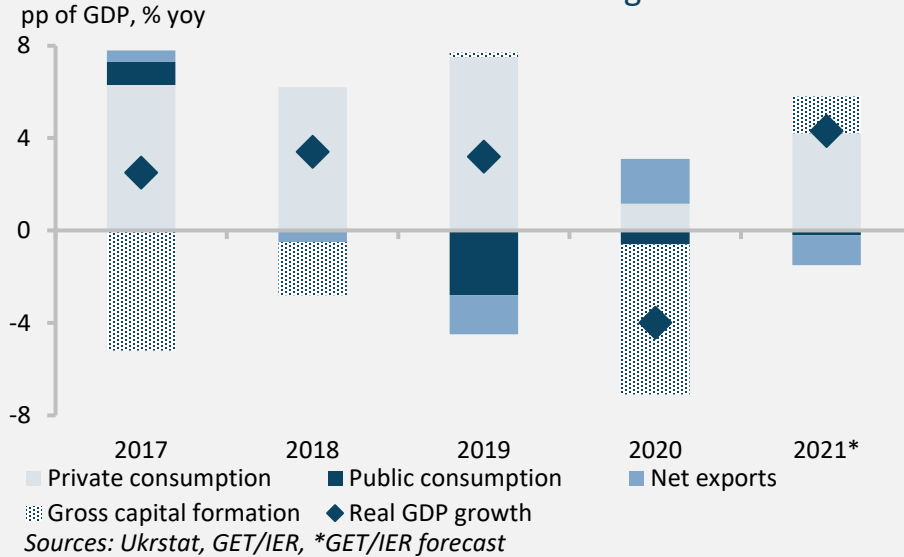
- 2020: GDP declined by 4.0%; less than expected
- 2021: Recovery expected with 4.3%
 - Impact of global/EU recovery
 - Domestic consumption growth
 - Good agricultural harvest
- From 2022: Return to moderate pre-crisis growth rates

International comparison

- Decline in 2020 was similar to peers
- Comparatively quick recovery: Pre-crisis GDP level to be reached already in 2021
- **Sound macroeconomic policies during the past years support fast recovery**
- **More reforms needed to permanently raise growth rates**

Sectoral perspective

Contribution to real GDP growth



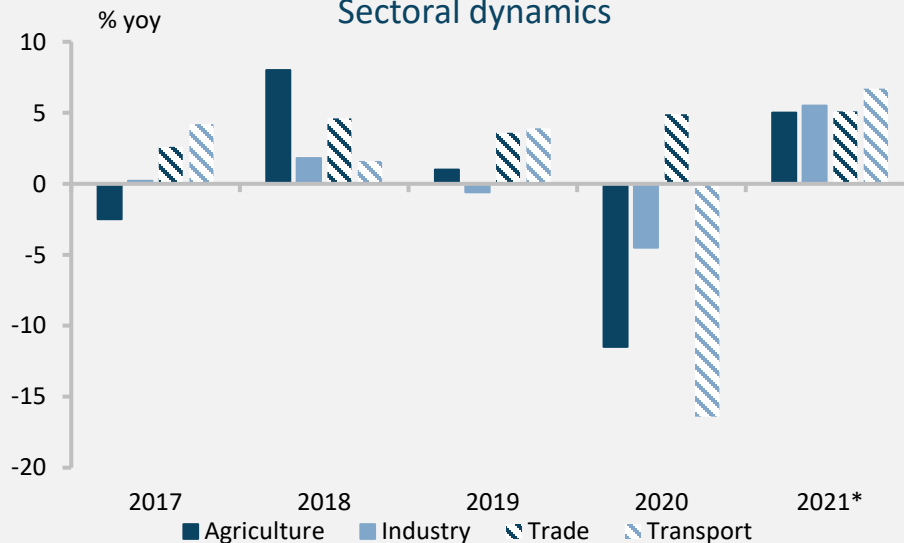
Demand side

- 2020: Investment was main driver of decline
- 2021: Private consumption and investment support economic recovery
 - Private consumption: 4.2pp. (growth contribution)
 - Investment: 1.6pp.
 - Negative contribution of net exports (-1.3pp.)

Supply side

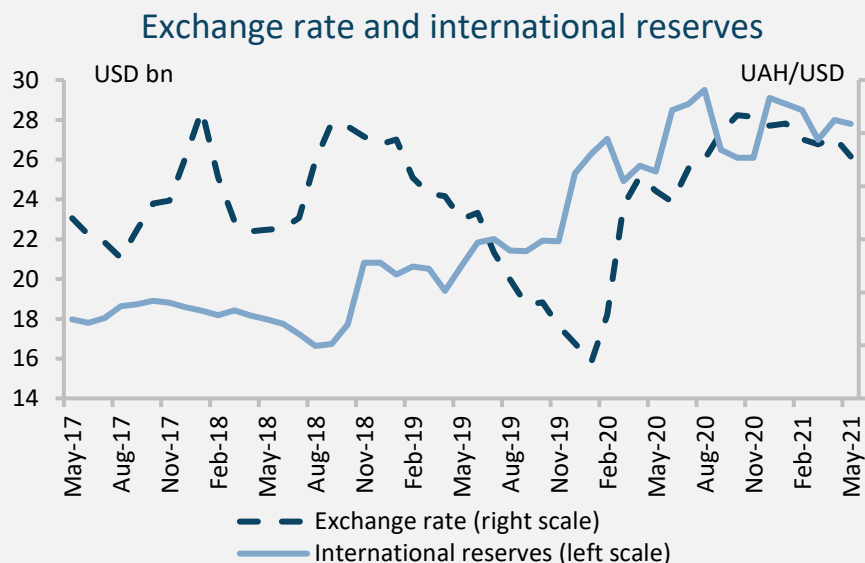
- 2020: Strong decline of industry and transport sector due to lockdown, agriculture due to bad harvest
 - 2021: Recovery expected across all sectors
 - Resumed strong production
 - Good weather conditions for agricultural harvest
- **Investment and private consumption resume role as drivers of growth**
- **Economic recovery across all main sectors**

Sectoral dynamics

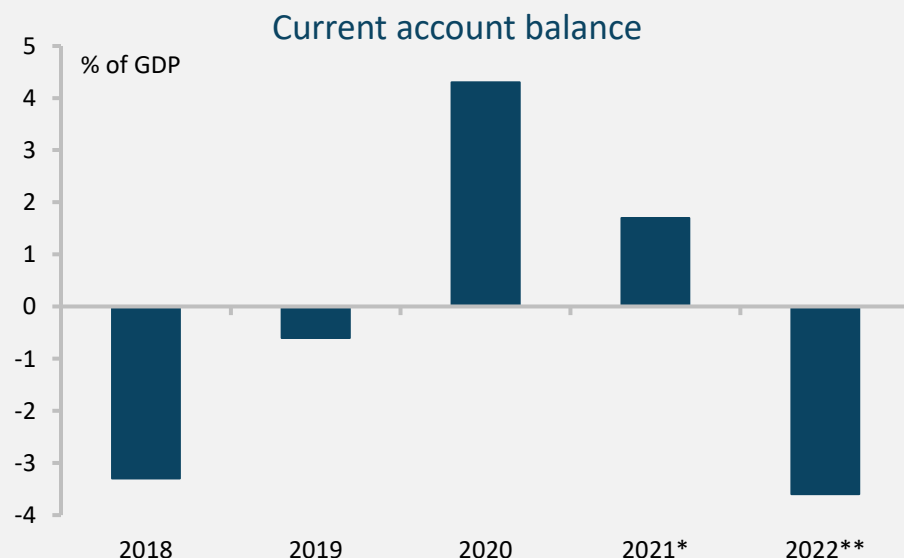


Sources: Ukrstat, GET/IER, *GET/IER forecast

Exchange rate and current account



Source: NBU



Sources: IMF, GET/IER, *GET/IER forecast, **IMF forecast

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Exchange rate

- 2020: Depreciation to UAH/USD 28.3 (19%)
- 5M2021: Relatively stable, slight appreciation to UAH/USD 27.6 (3.3%)

International reserves

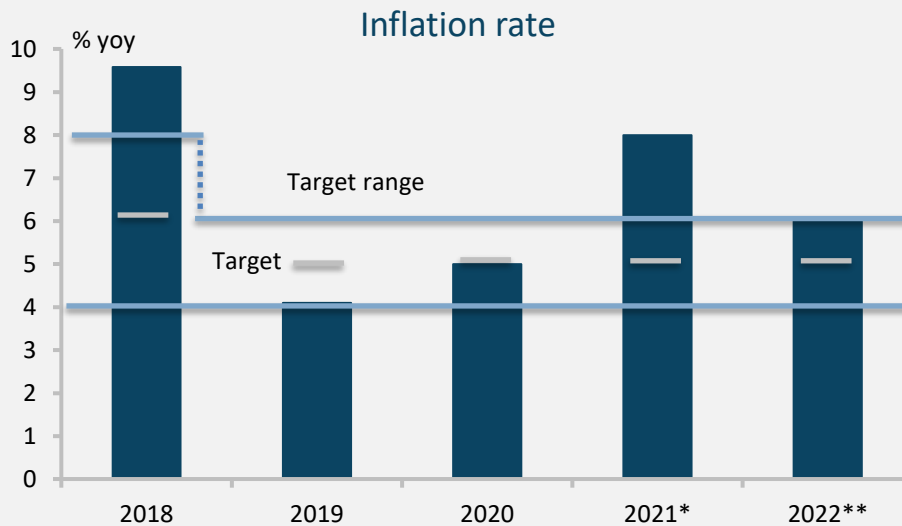
- 2020: Gradual accumulation despite crisis
- May-21: Reserves stable at USD 27.8 bn, import coverage: ca. 4.2 months

Current account

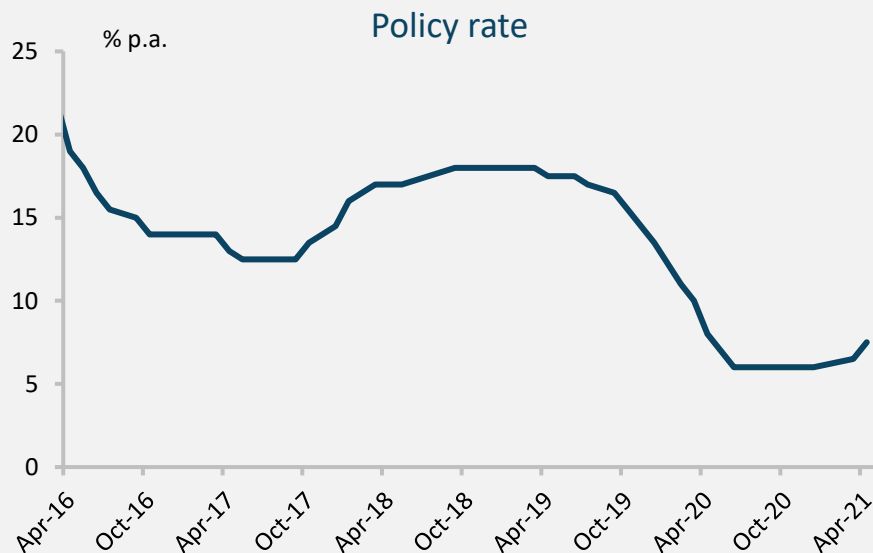
- 2020: Substantial surplus during the crisis
- 2021: Slight surplus (favourable terms of trade)
- 2022: Return to moderate structural deficit

- **Very solid external position supports recovery**
- **Flexible exchange rate important for shock absorption**

Inflation and monetary policy



Sources: NBU, IMF; note: end of period, *NBU forecast, **IMF forecast



Source: NBU

Inflation

- End of 2020: Inflation at 5%
- May-2021: Inflation sharply increased above the target range (4% to 6%) to 9.5%
 - Main drivers: Energy and food prices
 - Also supported by expansionary fiscal policy
 - Food prices expected to decelerate in 2H
- 2022: Return to target range expected

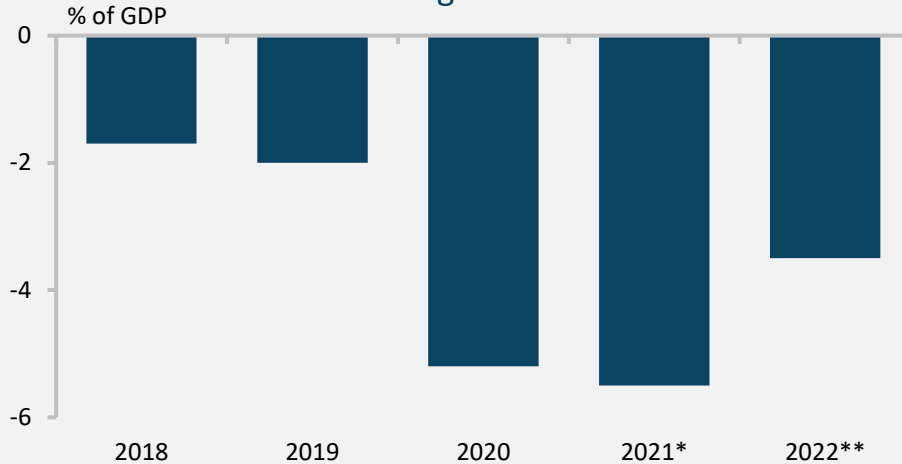
Policy rate

- Policy rate was reduced to 6% during the crisis, a historic low
- In April, increase to 7.5% due to rising inflation
- NBU indicates further hikes to bring inflation back under control

- **After monetary support during the crisis, the focus is now back on fighting inflation**
- **Independence of the central bank remains essential to bring inflation back to target**

Public finances

Budget balance

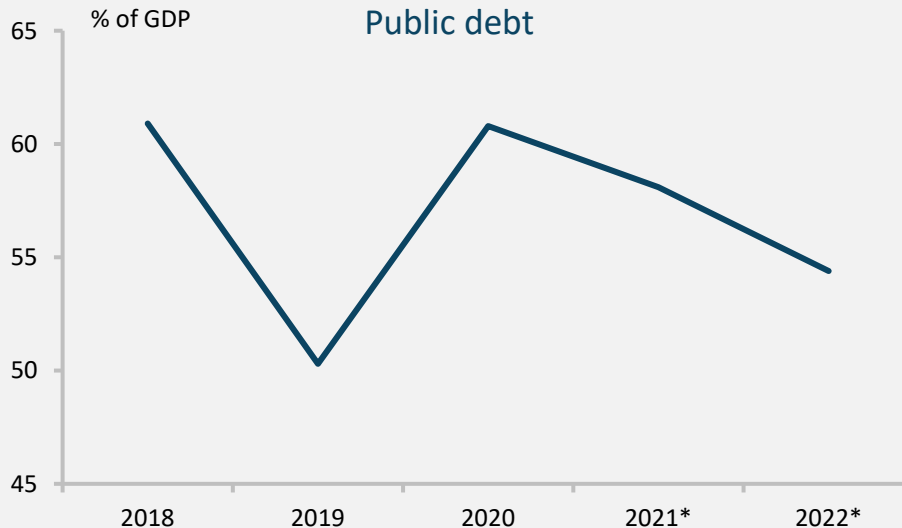


Sources: Ministry of Finance, IMF, *Planned deficit in the budget law, **IMF forecast

Budget

- 2020: Deficit at 5.2% of GDP
- 2021: 5.5% deficit planned despite economic recovery
- Actual deficit expected at ca. 4.5% of GDP due to stronger revenues during recovery
- Financing challenging without IMF programme
- Planned SDR allocation for all IMF members might ease pressure (USD 2.7 bn for Ukraine)

Public debt



Sources: Ministry of Finance, IMF, *IMF forecast; note: debt incl. state-guarantees

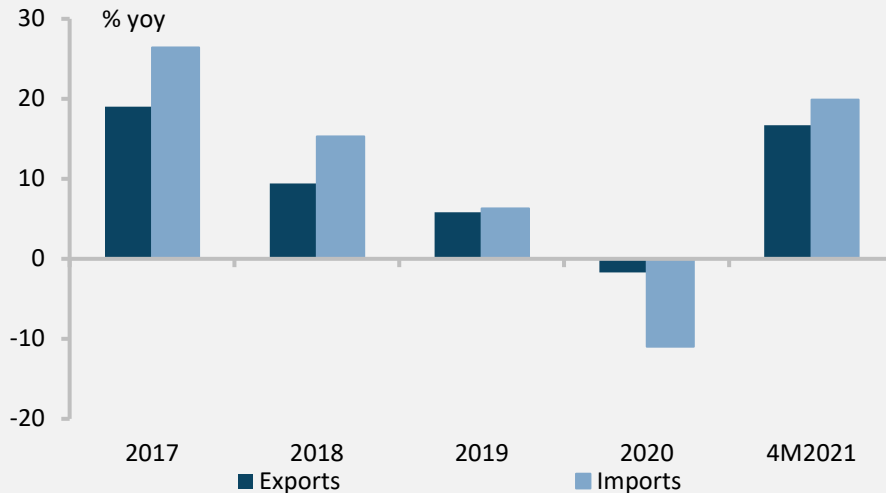
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- 2020: Significant increase of debt ratio (60.8%)
- Debt ratio declining due to GDP recovery from 2021, assumes consolidation in future years
- GDP warrants: First payment of USD 41 m in May, substantial contingent liability in future

- **Pre-crisis consolidation enabled fiscal support during the crisis**
- **IMF-programme remains important**
- **Return to consolidation required in 2022**

External trade

External trade



Sources: Ukrstat, NBU; note: trade in goods; data for April are preliminary

Exports and imports of goods

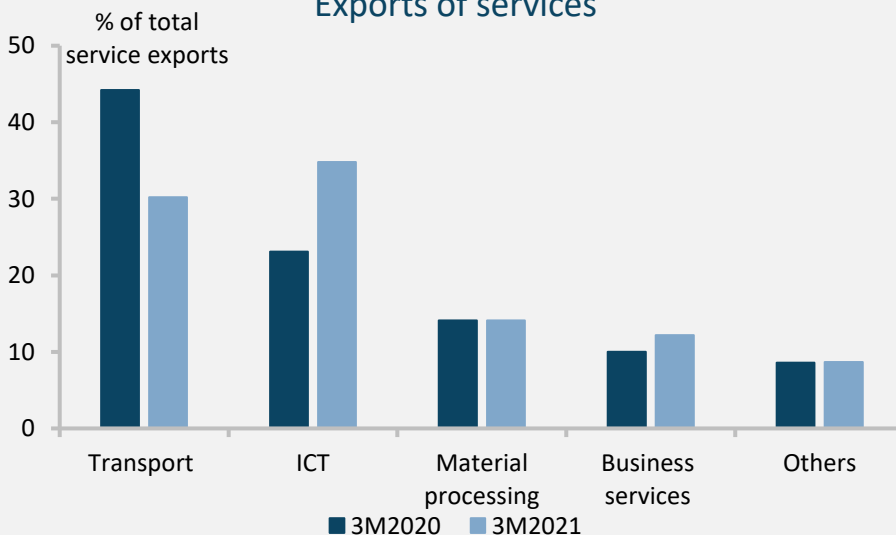
- 4M2021: Sharp recovery of trade (18%) in both exports and imports (17% and 20%)
- Exports: Rebound driven by metal and minerals exports (39% and 69%) mainly due to high prices
- Imports: Main driver are machinery imports (28%) in tune with investment recovery

Exports of services

- Service exports make up 15% of total exports
- Decline by 14% in 3M2021 due to baseline effect
- ICT now most important service export sector (35%), transport (incl. pipelines) is next (30%)

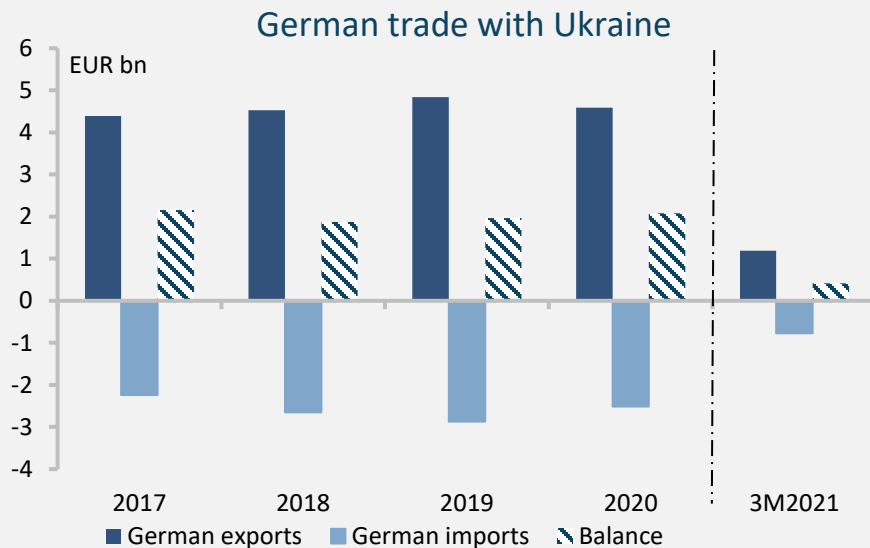
- **Quick recovery of goods trade after the crisis**
- **Service exports will recover during 2021**
- **Growth of ICT-exports continues**

Exports of services



Source: Ukrstat
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Bilateral trade between Germany and Ukraine



Source: Federal Statistic Service, 3M2021; note: trade in goods

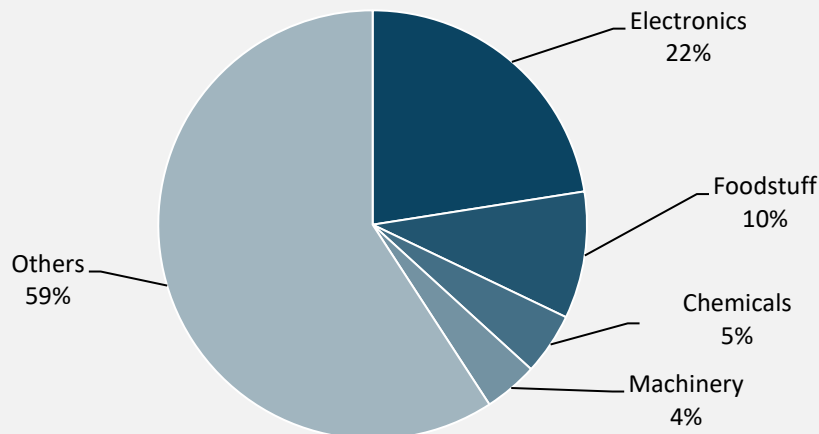
Bilateral trade

- Considerable decline by 7.9% in 2020
- Rebound by 4.8% after 3M2021

German exports to Ukraine

- 3M2021: Exports declined by 1.3%
- Traditional export products: Chemicals (22%), machinery (incl. agricultural machines) (21%), motor vehicles (incl. parts) (14%)

Structure of German imports



Source: Federal Statistic Service, 2020; note: trade in goods

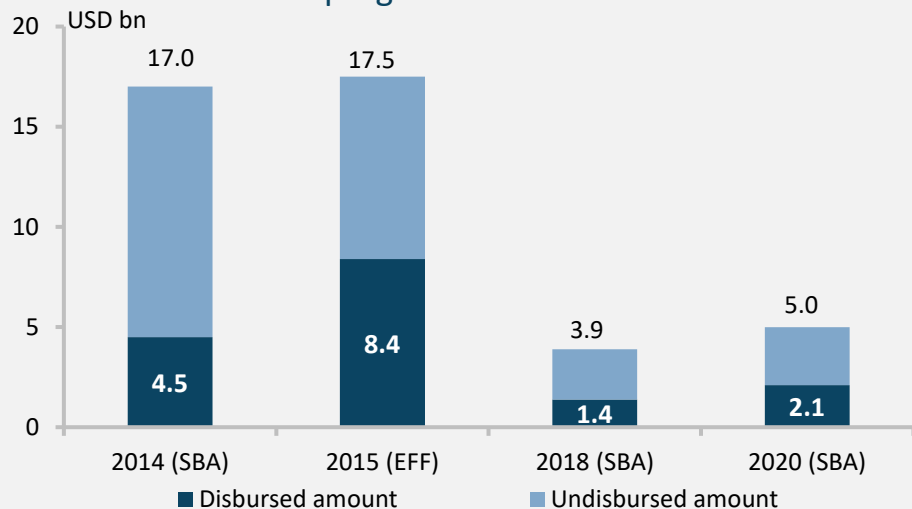
German imports from Ukraine

- 3M2021: Strong increase of imports by 15.8%
- Increase driven by foodstuff imports (53%) and machinery (32%)

➤ **Moderate recovery of bilateral trade in 2021 driven by German imports from Ukraine**

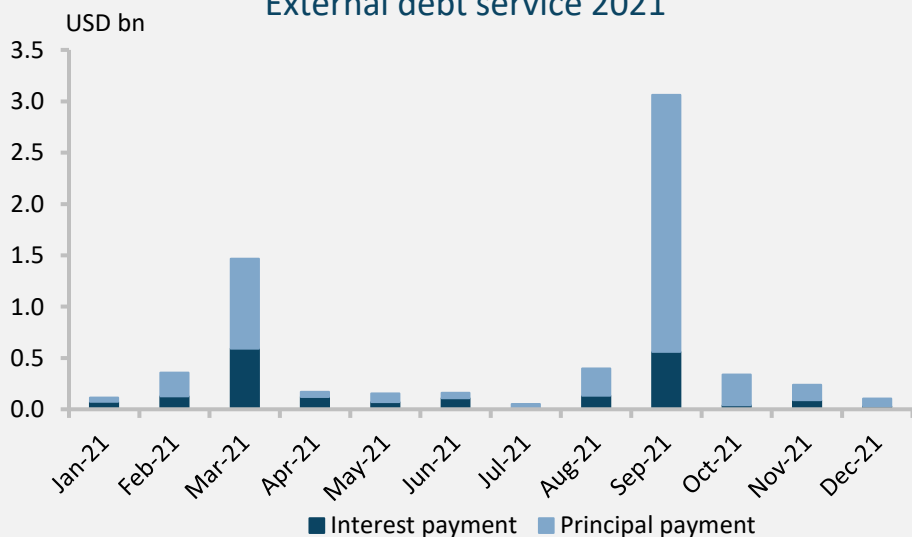
Current IMF programme

IMF programmes since 2014



Source: IMF

External debt service 2021



Sources: Ministry of Finance, IMF, NBU, own calculation

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Background

- COVID-19 led to a new “Stand-by-Arrangement” (SBA) in June 2020
 - Duration: 18 months; Volume: USD 5 bn
 - USD 2.1 bn disbursed in June 2020
- Feb-21: IMF review mission ended without staff level agreement due to lack of reform progress and some setbacks

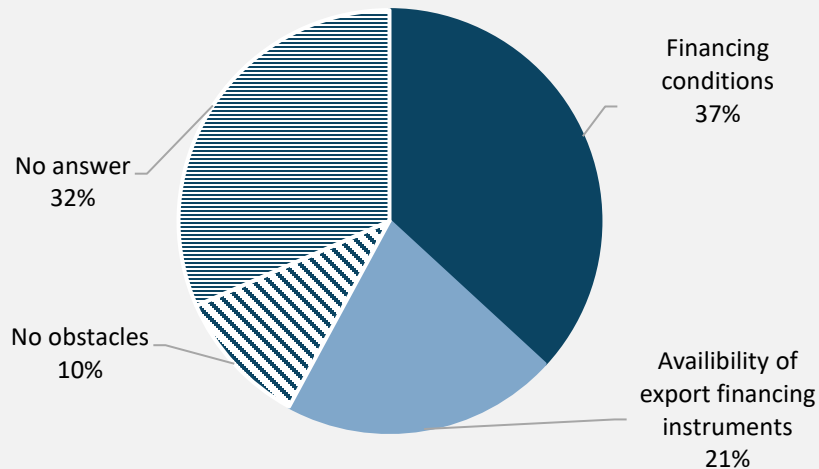
Importance of the IMF-programme

- IMF programme remains vital as conditionality for other donors’ programmes
- Financing of deficit might become difficult without further IMF-financing as total external debt service is USD 6.6 bn in 2021

- **Positive steps in different areas are essential for further cooperation with the IMF**
 - **Anti-corruption agenda**
 - **Judicial reform**
 - **Energy tariffs**
 - **Corporate governance of SOEs**
 - **Independence of the National Bank**

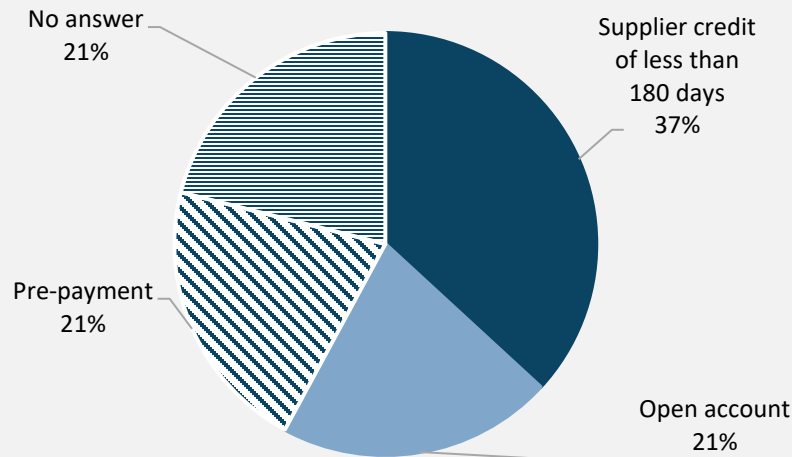
Export finance

Obstacles in the use of bank export financing



Source: Own survey; note: no answer may refer to non-exporting companies

Payment terms in export finance



Source: Own survey

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Background

- State export support is key instrument for strengthening Ukrainian exports and competitiveness
- GET conducted an enterprise survey on obstacles in export finance, together with AHK Ukraine and Ukrainian Chamber for Commerce

Results

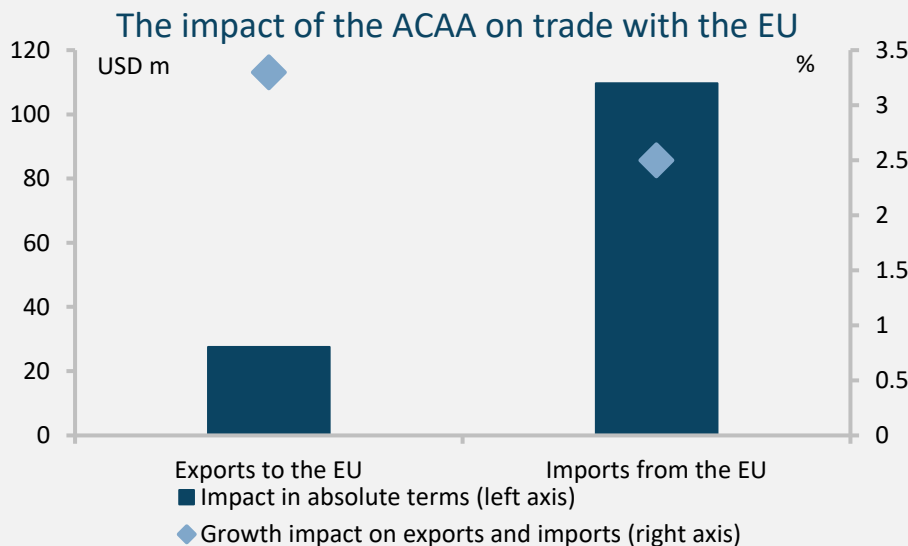
- 58% of companies report obstacles:
 - Unavailability of export finance by banks
 - Payment risks of potential buyers
 - Taxes and customs services
 - No availability of middle- or long-term supplier credits (>180 days) but manufacturing goods require longer payment terms
- **Lack of support by the export credit agency (ECA) and commercial banks**
- **Need for an efficient and sufficiently capitalised ECA to cover risks from the banking sector**

ACAA with the EU

Ukraine's progress on the road to ACAA

	Legislation	Quality infrastructure
Step 1: Alignment to EU norms	✓	✓
Step 2: EU pre-assessment mission	✓	← ongoing
Step 3: Implementing recommendations	← ongoing	
Step 4: Official assessment		
Step 5: Formal negotiation & conclusion		

Source: Own illustration; note: step 2 and 3 might be repeated until full alignment



Source: Own estimates; percentage impact on goods categories covered by ACAA

ACAA is a key political priority of Ukraine

- Agreement on Conformity Assessment and Acceptance of industrial products
- Further reduces non-tariff barriers to EU-Ukraine trade in 3 (out of 27) product categories
- “Internal market treatment” for covered Ukrainian industrial goods in EU

Progress by Ukraine

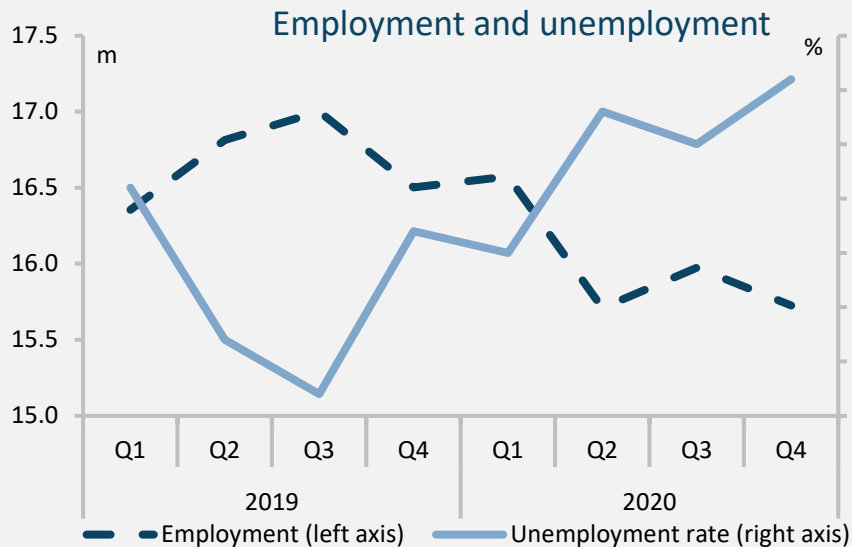
- Legislation alignment at advanced stage, EU pre-assessment mission submitted report in spring 2021
- More work likely to be needed to ensure alignment of quality infrastructure (institutions)

➤ **Positive, but small direct effect on trade (+ USD 27.5m of exports, USD 109.7 m of imports)**

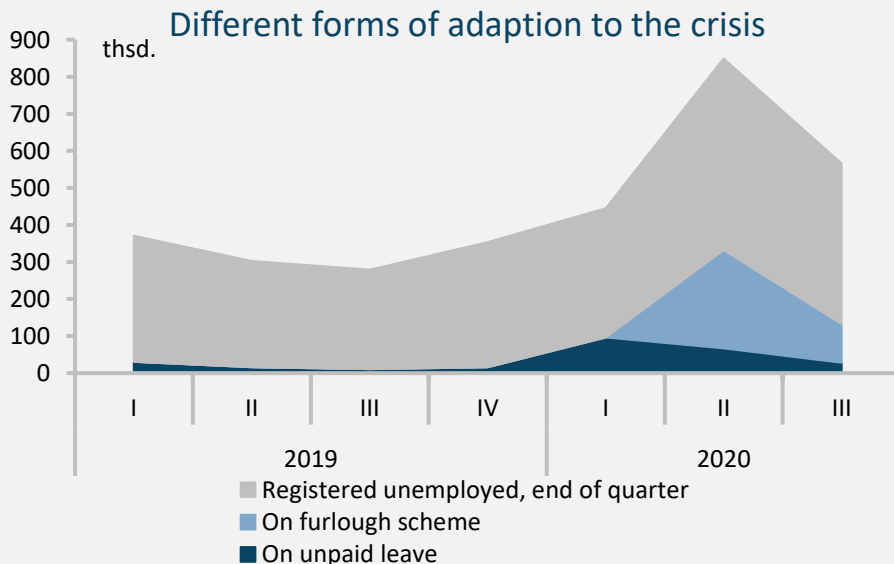
➤ **Indirect effects will matter more:**

- **Extending trade to new products and new companies**
- **Signal of quality for other markets**
- **FDI attraction and stronger integration in the EU market**

Labour market reaction to the pandemic



Sources: Ukrstat, NBU



Sources: Ukrstat, State Employment Service

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Challenge

- Companies needed to quickly cut costs following a simultaneous demand and supply shock

Government measures

- Labour law package (adapted regulations on unpaid leave, remote work etc.)
- Modification of short-time work scheme
- UAH 8,000 per worker paid twice to companies affected by lockdown

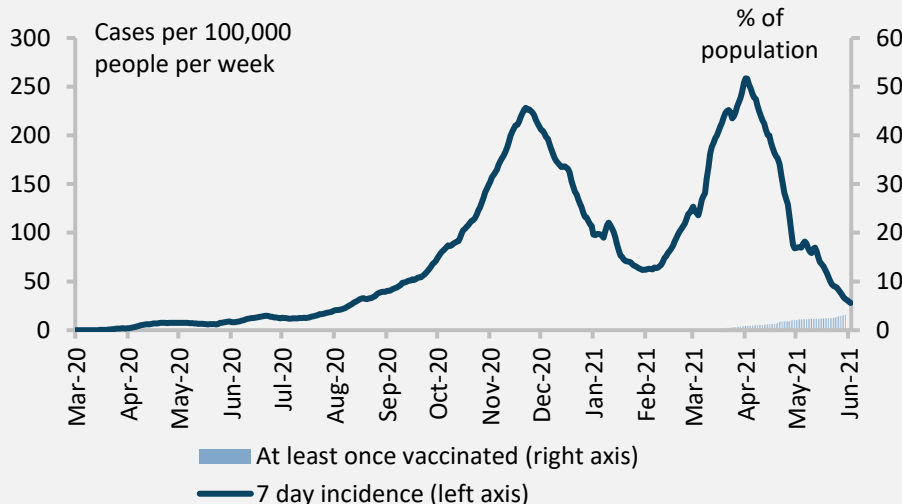
Reaction of companies

- Unpaid leave (in cooperation with workers) used by some companies
- Short-time work scheme was only available to SMEs closed by lockdown regulations

- **Despite firing costs and need for workers post-pandemic, layoffs were main reaction**
- **Extending the short-time work scheme may be beneficial for faster recoveries in future**

COVID-19: Overview of cases

7 day incidence and vaccination



Sources: Our World in Data, Ukrstat, own calculation

Incidence and vaccination in international comparison

	7 day incidence	Vaccinations (% of pop)	
		Min. once	full
Ukraine	31	3.0	<1.0
Poland	8	39.2	22.8
Belarus	63	5.5*	3.0*
Georgia	141	4.5	1.3
Russia	44	12.2	9.3
EU-27	42	41.7	21.5
Germany	24	46.5	22.8

Sources: Johns Hopkins University, Our World in Data, data as of 8 June 2021, 7 day incidence per 100,000 people, vaccination data for for Belarus from 30 May 2021

Domestic perspective

- Incidence is on declining path (Avg. Jun-21: 35)
- However, vaccination programme is at very low level, no positive impact on economic recovery
- Vaccines received through COVAX (AstraZeneca, Pfizer/BioNTech) and bilateral agreements (Sinovac)
- Long way to go before mass vaccination

International perspective

- 7-day incidence is moderate in regional comparison
- However, EU have already begun with mass vaccination

- Incidence declining in summer
- Lack of vaccine doses causes slow start of vaccination programme

About the German Economic Team



Financed by the Federal Ministry for Economic Affairs and Energy, the German Economic Team (GET) advises the governments of Moldova, Georgia, Ukraine, Belarus and Uzbekistan on economic policy matters. Furthermore, GET covers specific topics in other countries, such as Armenia. Berlin Economics has been commissioned with the implementation of the consultancy.

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