



Economy review in January.

Special topic: Government vs Business. How to ease pressure on Ukrainian entrepreneurs?



EXECUTIVE SUMMARY

EXECUTIVE SUMMARY: UKRAINIAN ECONOMY IN JANUARY 2024

- **SPECIAL TOPIC:** Business is outraged by the growing pressure from the state. The government promises to halt all “masquerade shows”, breaks its promise a couple of weeks later.
- **MACROECONOMIC TRENDS:** GDP grew by 5.7% in 2023, but the recovery will slow down in 2024 and further. Business confidence, as well as consumer confidence, is waning.
- **SECTORAL ANALYSIS:** Ukrainian agricultural exports are high thanks to the Sea corridor and attribute to record-high overall exports. Ukraine energy system is stable, as well as ferrous production – albeit far from pre-war levels.
- **MONETARY AND FX SECTOR:** Inflation slows down even further; international reserves are high, and the key rate is stable.
- **BANKING SECTOR:** Banks are faring rather well, with liquidity on its highest level, lending rates demonstrating downward trend, and loans and deposits on the rise.
- **FISCAL SECTOR:** With only \$0.4 bn of foreign financing in January, Ukraine had to postpone its budget expenditures to survive the month.

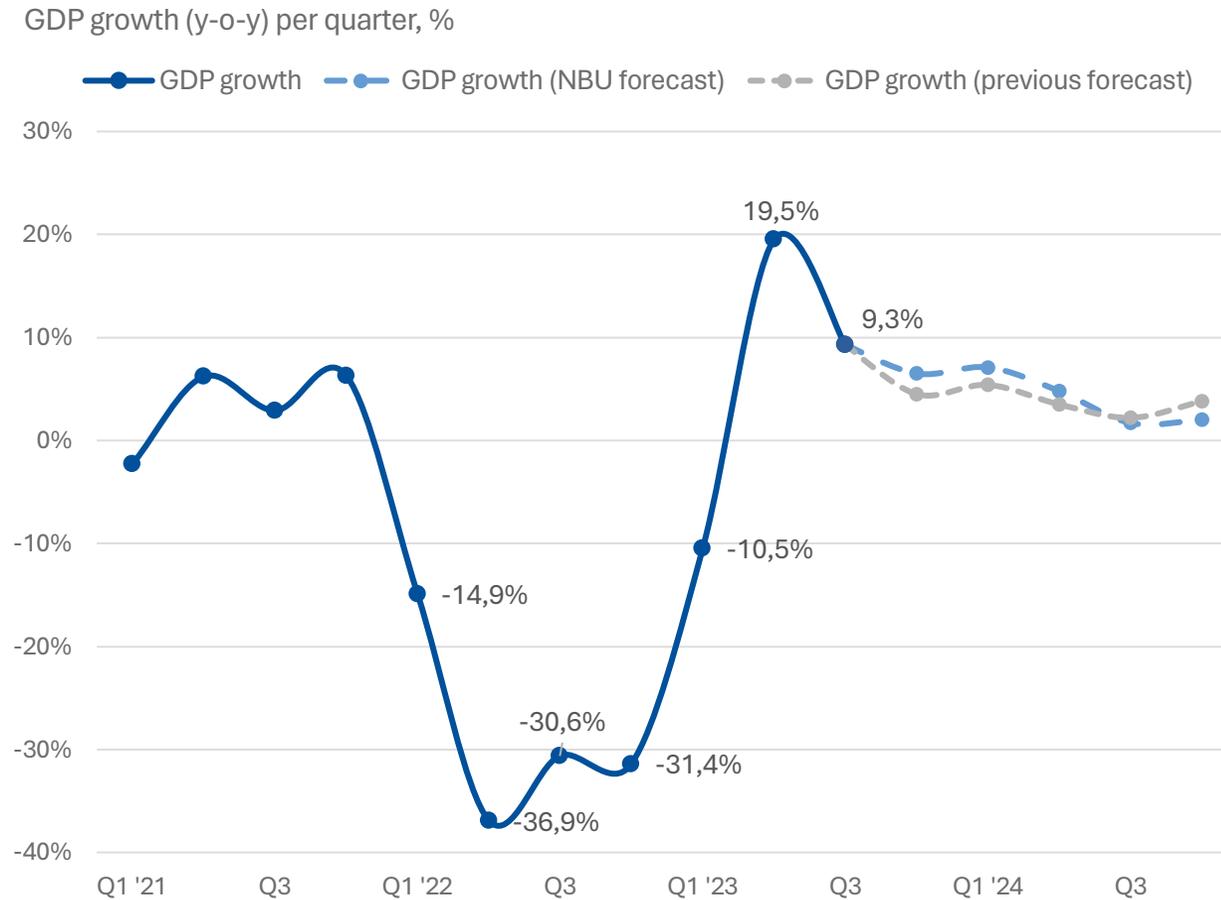
See our report below for further details.



MACROECONOMIC TRENDS

MACROECONOMIC TRENDS

GDP growth (recovery) will slow down in 2024 and further

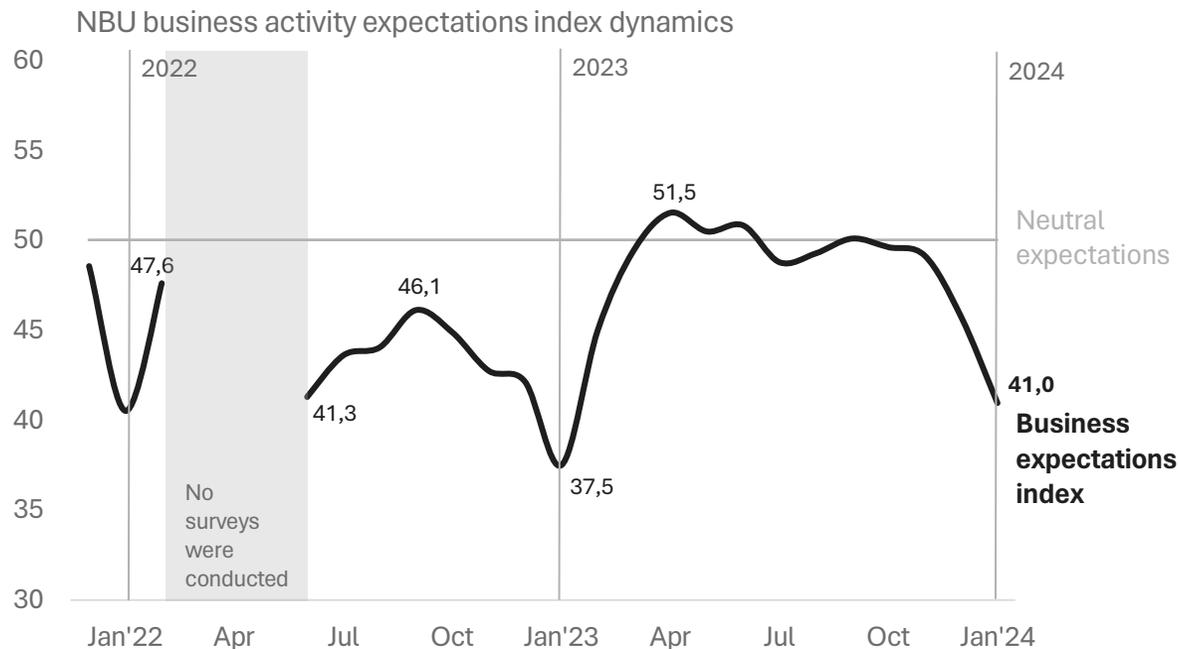


- In 2023, GDP of Ukraine grew by 5.7% (NBU estimate), an improvement from 4.9% in previous forecast.
- The NBU estimates that GDP grew by 6.5% in Q4 2023.
- According to the same forecast, Ukraine's GDP will grow by 3.6% in 2024 and by 5.8% in 2025.
- The NBU believes that the key prerequisite for economic recovery next year is the reduction of security risks.

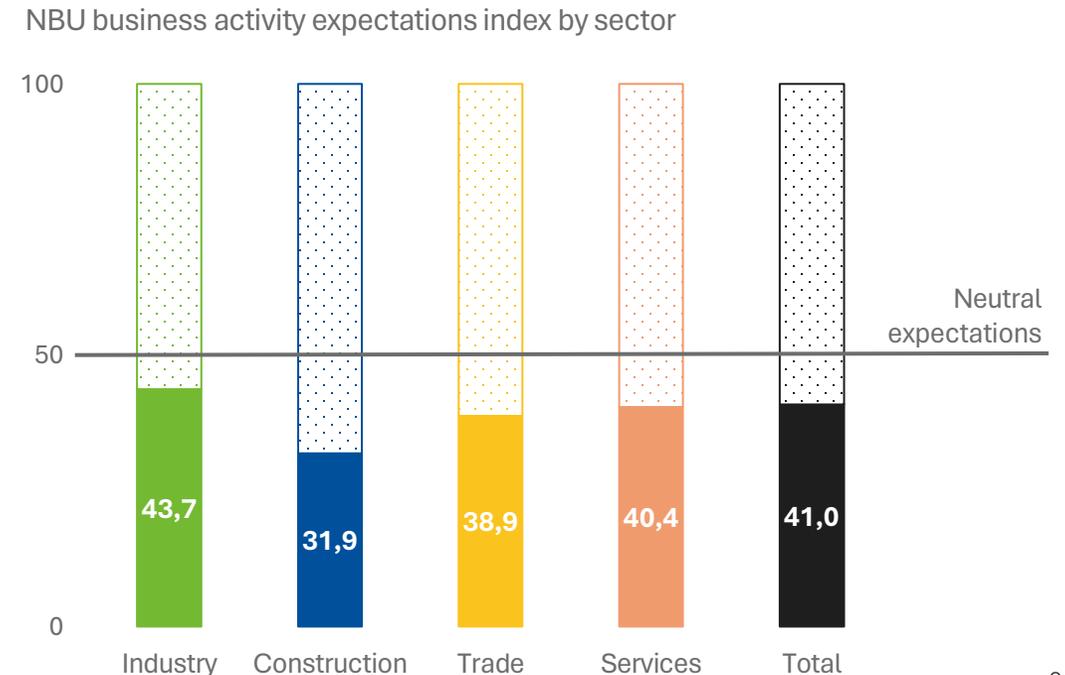
MACROECONOMIC TRENDS

Business expectations are worsening

- In January, NBU business activity expectations index was 41.0 — expectations were negative. **Business expectations continued to fall for the fourth month in a row and are now lower than in the first months of the full-scale war, but still higher than in January 2023.**
- **All sectors reported negative expectations.** Increased intensity of hostilities, uncertainty about the timing and amount of external financial assistance, blockade of the western borders, increased production costs for strengthening cyber defense, lack of qualified personnel among the main reasons for pessimism.



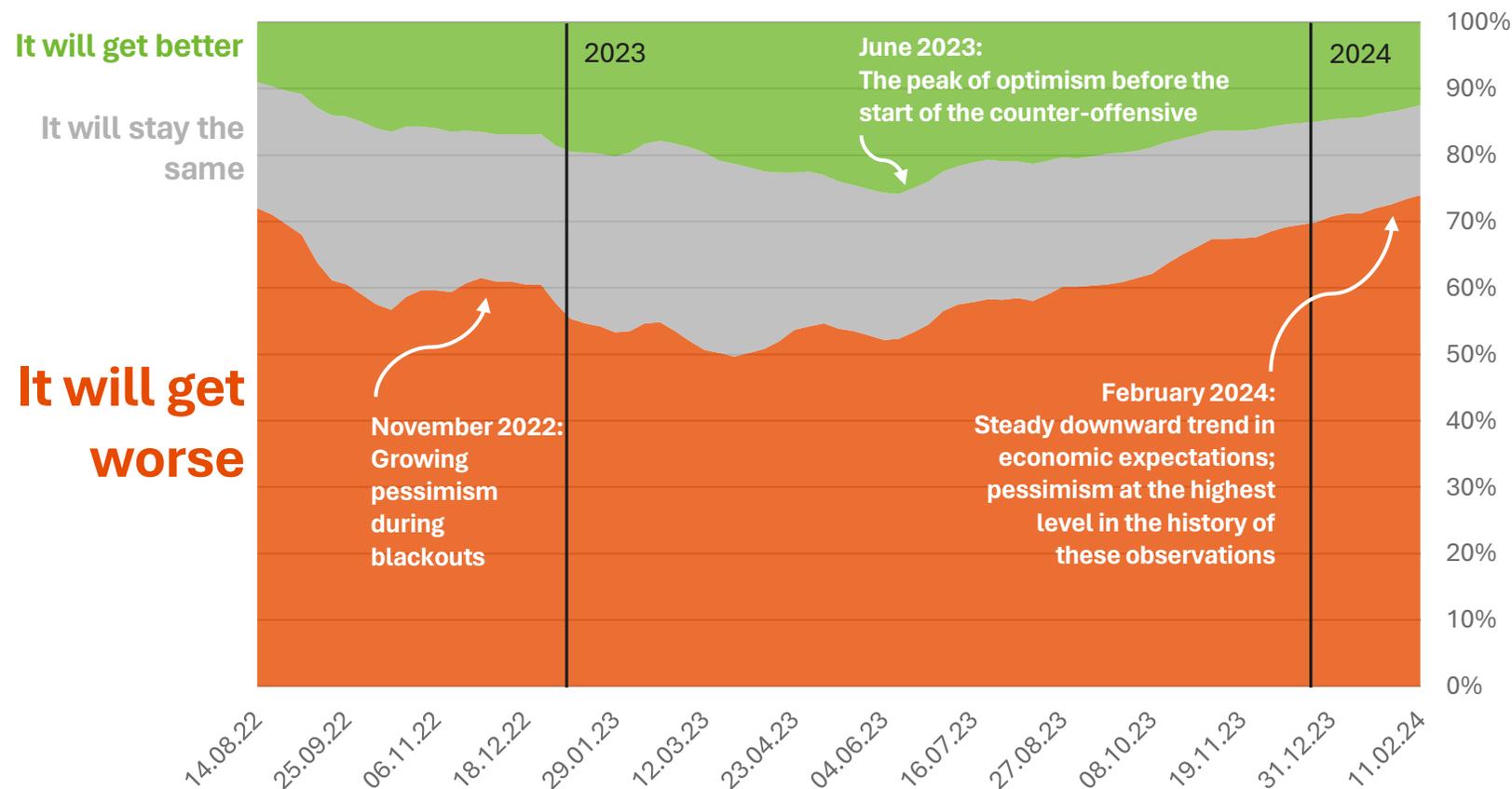
Source: NBU



MACROECONOMIC TRENDS

Economic expectations of the public are also worsening steadily

Results of the survey "What do you expect to happen to the economic situation in the country during the year?", tg-channel of MP Yaroslav Zheleznyak, 6-week moving average



Source: Yaroslav Zheleznyak (t.me/yzheleznyak), CES calculations

- The public also grows more pessimistic, with different surveys confirming the trend.
- For instance, the share of respondents that believe that the economic situation will get worse reached an all-time high of 77% according to regular survey conducted by Yaroslav Zheleznyak, MP.
- Consumer confidence index has also been steadily declining.

**БЮРО
ЕКОНОМІЧНОЇ
БЕЗПЕКИ УКРАЇНИ**

SPECIAL TOPIC: INCREASED GOVERNMENT PRESSURE ON BUSINESS

INCREASED GOVERNMENT PRESSURE ON BUSINESS

The problem

The current agenda:

1. Distinguishing between the fulfillment by the authorities of their statutory functions and their abuse to achieve unscrupulous political or property goals
2. Recently, government agencies have increased their influence on business, which is often perceived by the business environment as pressure

A lot of different forms of pressure

Signs of dishonesty by public authorities may include:

- Obviously **excessive investigative actions** in view of the date, scope and consequences of the alleged offenses
- **The use of force** and intimidation to obtain information that companies provide voluntarily at the first request of regulatory authorities.
- Creating **artificial obstacles** to doing business while offering informal ways to solve problems
- Excessive number of **business inspections**
- **Delaying the pre-trial investigation** to keep risks for companies
- Dozens of other forms

INCREASED GOVERNMENT PRESSURE ON BUSINESS

“Mazepagate” timeline

May 28, 2023

Concorde Capital founder Ihor Mazepa announces the creation of a rating of law enforcement officers and judges who use their powers for illegal purposes.

January 18, 2024

Ihor Mazepa is detained on the border of Ukraine and Poland. Concorde Capital was searched, and his brother Yuriy was detained.

January 23, 2024

Kyiv Court of Appeal reduces the bail to UAH 21 million. This amount was paid, and Ihor Mazepa was released.

January 23, 2024

President Volodymyr Zelenskyy reacts in his daily address: he announces a moratorium on "mask shows," the creation of the Entrepreneurship Support Council, and amendments to the law on the Bureau of Economic Security.

June 29, 2023

Mazepa's initiative is joined by 41 other entrepreneurs. The movement was called Manifesto 42.

January 19, 2024

The court imposes a pre-trial restraint on Ihor Mazepa in the form of detention with an alternative bail of UAH 349 million, ten times the amount of the alleged damage to the state.

January 23, 2024

Mazepa states that the events of the case against him took place in 2013, but the case started moving only a 1,5 months ago. He attributed his detention to the activities of the Manifesto 42.

January 26, 2024

President issues a decree establishing the Council for Entrepreneurship Support. Out of its 7 members, most are media personalities, and most are representatives of IT sector.

INCREASED GOVERNMENT PRESSURE ON BUSINESS

Council for Entrepreneurship Support: reflections

- **Yulia Svrydenko, Minister of Economy of Ukraine:** «The key message is that the economic bloc of the government and business are on the same side. I am ready to fight for every entrepreneur personally. After discussions with business, in the government circle, and at the National Security and Defense Council, President Volodymyr Zelenskyy announced practical steps that could stabilize the situation. The ultimate goal is to establish additional guarantees to protect business interests during searches and other procedural actions».
- **Volodymyr Mnoholetniy, co-founder and CEO of Genesis:** «Just a couple of days after the Mazepa case, the National Security and Defense Council met and made a number of important decisions. A moratorium on business inspections, the creation of a single body responsible for inspections, and limiting the ability to put pressure on business. It is clear that everything will depend on implementation, but this is a very important and very quick step in the right direction».
- **Halyna Yanchenko, MP/ Sluha Narodu:** «We, on behalf of the Parliamentary Special Commission on Investor Protection, will prepare our list of strange criminal cases against business and pass it on to the security forces. The bad news is that the proposed solutions are not enough. They will not solve the problem of raids on business globally and in the long term. Additional actions are needed».
- **Yaroslav Zheleznyak, MP/Holos:** «None of those involved in the Mazepa case and other high-profile cases has even been punished. All that remains is profanation and imitation. The systemic changes insisted on by entrepreneurs have not been proposed».

Older cases



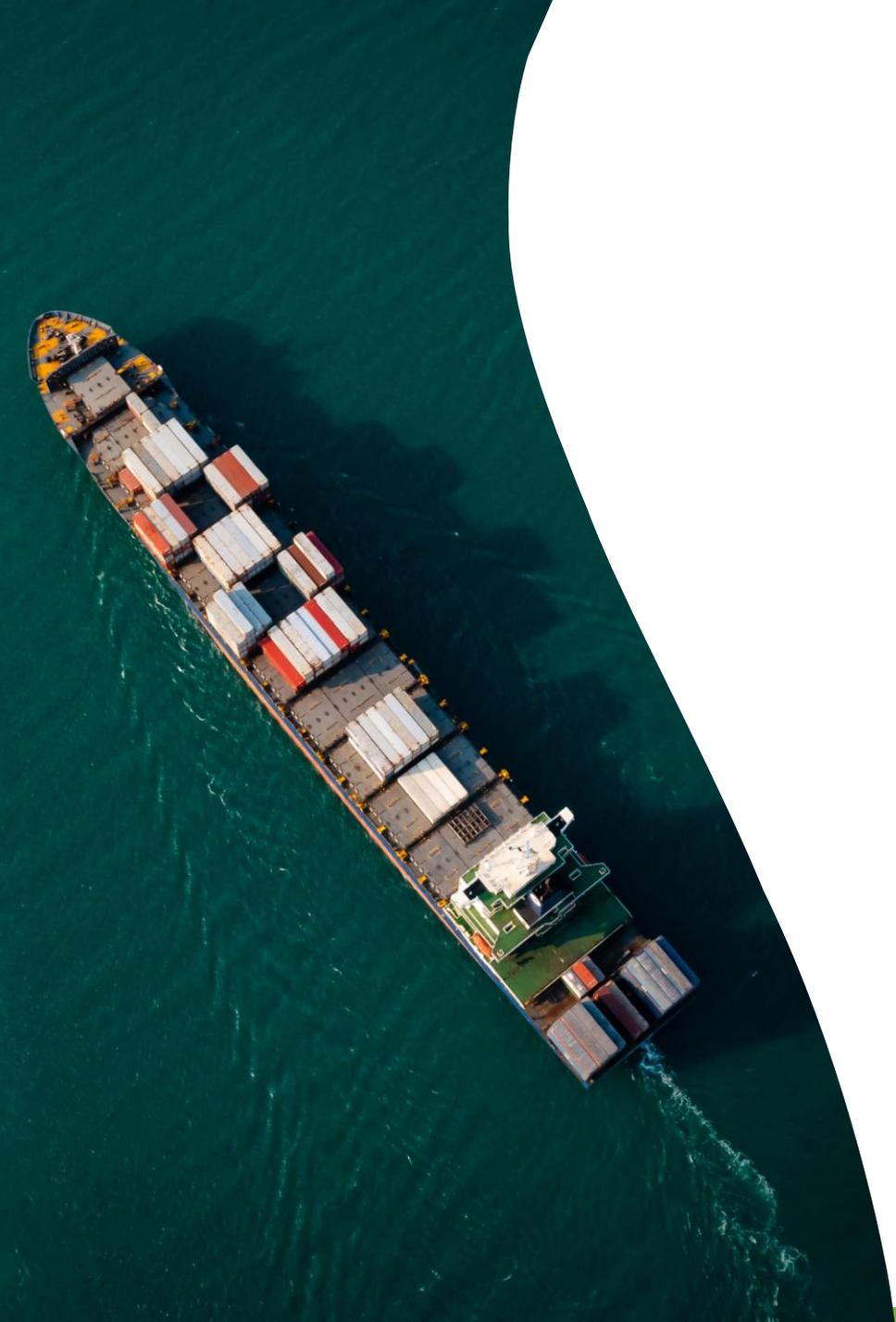
2021- Nova Post received a fine of UAH 326 million from the State Consumer Service. The formal reason was "obstruction of inspection". After public outcry, the fines were canceled as disproportionate.



2022 - Rozetka owner Vladyslav Chechotkin stated that on average, the company receives more than 10 inspections per month. The inspections usually result in small but numerous fines.



2023 - Oleksandr Kosovan's company MacPaw was searched. The stated reason was violations in obtaining land for the construction of the MacPaw Village recreation center. According to the businessman, the real reason is the desire of law enforcement officers to take possession of these lands.



SECTORAL ANALYSIS

SECTORAL ANALYSIS

Ukraine's exports sets records, in physical terms so far

- In January 2024, Ukraine reached a record high for physical exports during the large-scale invasion - 12 million tons of products, only 2 million below January 2022. More than 72% was exported by sea.
- In USD terms, exports increased to \$3.4 bn, the highest in the last 10 months, while imports decreased to \$4.8 bn. As a result, the current account deficit of the trade balance decreased to \$1.4 billion.
- The key deterrents to Ukraine's foreign trade remain the danger of shipping in the Black Sea and the blocking of Ukrainian supplies at the EU borders, primarily in Poland.

Import and export of goods, \$ bn



Source: Ministry of Economy

SECTORAL ANALYSIS

Ukraine energy system is back in balance in mid-February

- In 2024, the power system has been operating consistently, with a moderately high load. Disruptions in the power system are local and are quickly eliminated.
- While in January, power outages were primarily caused by weather conditions, recently they have been caused by Russian shelling near the state border or the front line.
- According to the latest information, 386 settlements and more than 70,000 consumers in the government-controlled area remain without access to electricity.
- In January, commercial net imports almost halved m-o-m to 117 GWh. At the end of the first decade of February, the system was balanced and Ukrainian electricity exports to Moldova, Poland, Romania, and Moldova resumed.

Ukraine net electricity commercial exports in 2023-2024, GWh

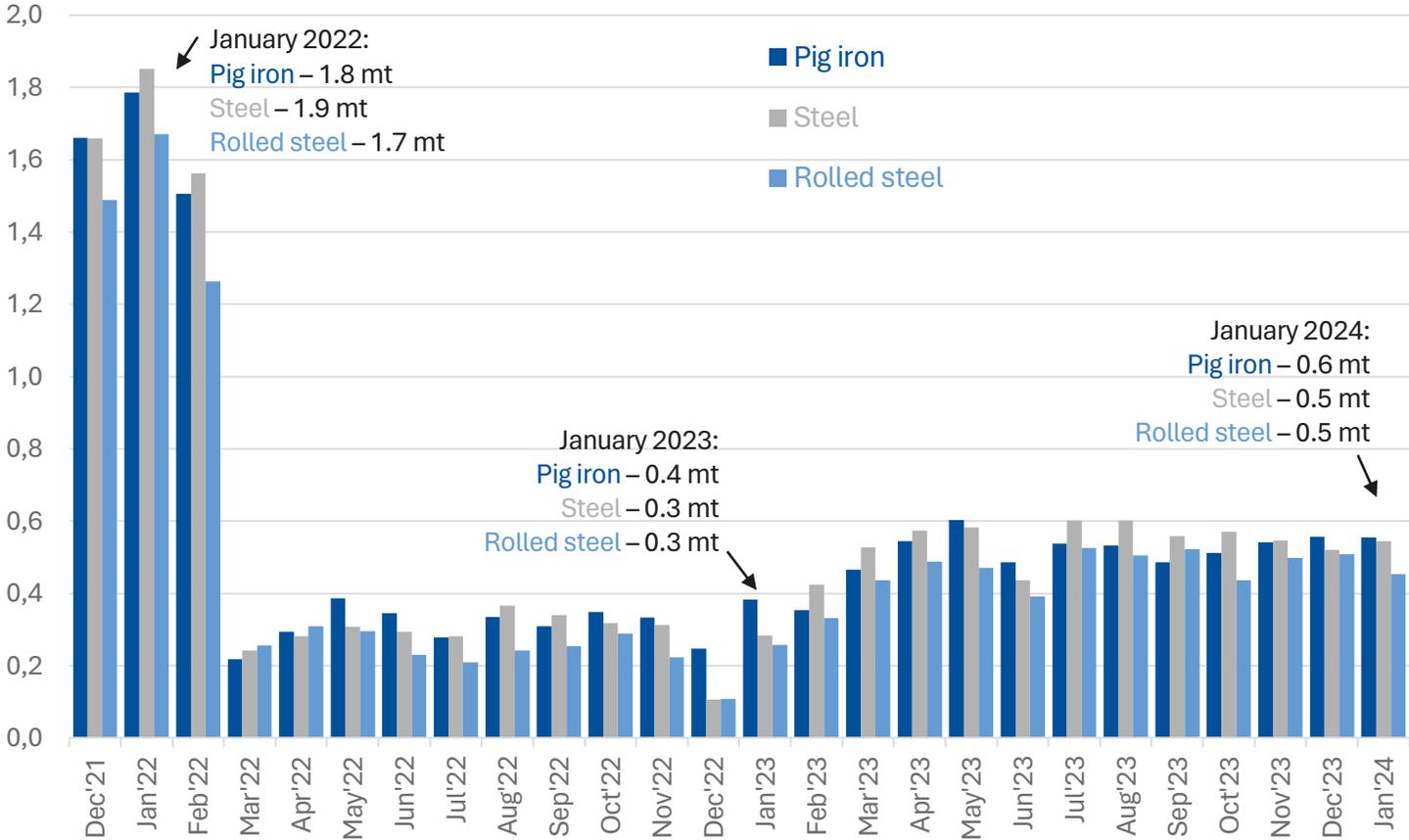


Sources: ENTSO-E

SECTORAL ANALYSIS

Ferrous production keeps the tempo, far from pre-war volumes

Ukraine ferrous production by main categories, mt



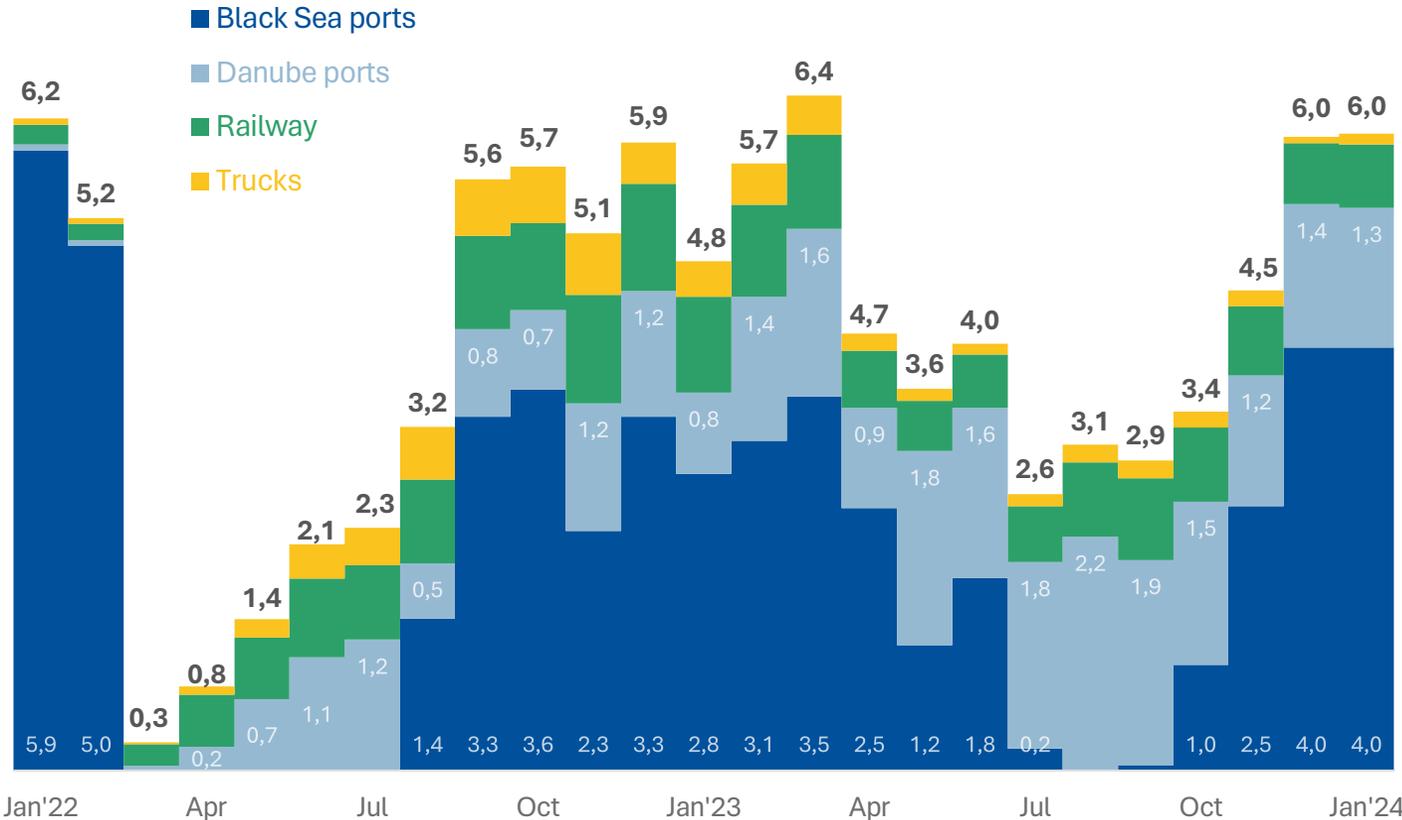
Source: Ukrmetallurgprom

- In January, steel production decreased by 0.3% m-o-m to 555 thousand tons, while pig iron production grew 4.5% to reach 544 thousand tons (+4.5%), and rolled products output shrank 10.9% to 453 thousand tons.
- Although output volumes are three times lower than before the full-scale invasion, they are 1.5-2 times higher than in January 2023.
- Steel consumption in Ukraine increased by 20% in 2023, primarily due to the implementation of government projects.
- In 2023, scrap metal procurement increased by 28% to 1.27 mt, while scrap supplies to steel mills increased by 15% to 1.03 mt. In 2024, market participants expect growth rates to continue, but the figures will remain far from the volumes of 2021.
- In 2023, Ukraine exported 344 thousand tons of ferroalloys worth \$298 million. While the annual decline in physical volume was 5%, the annual decline in monetary terms was 49%. The main export destinations are Poland (53%) and Turkey (14%).

SECTORAL ANALYSIS

Agri exports remains at December highs

Exports of grain and oilseeds by transport and total, million t

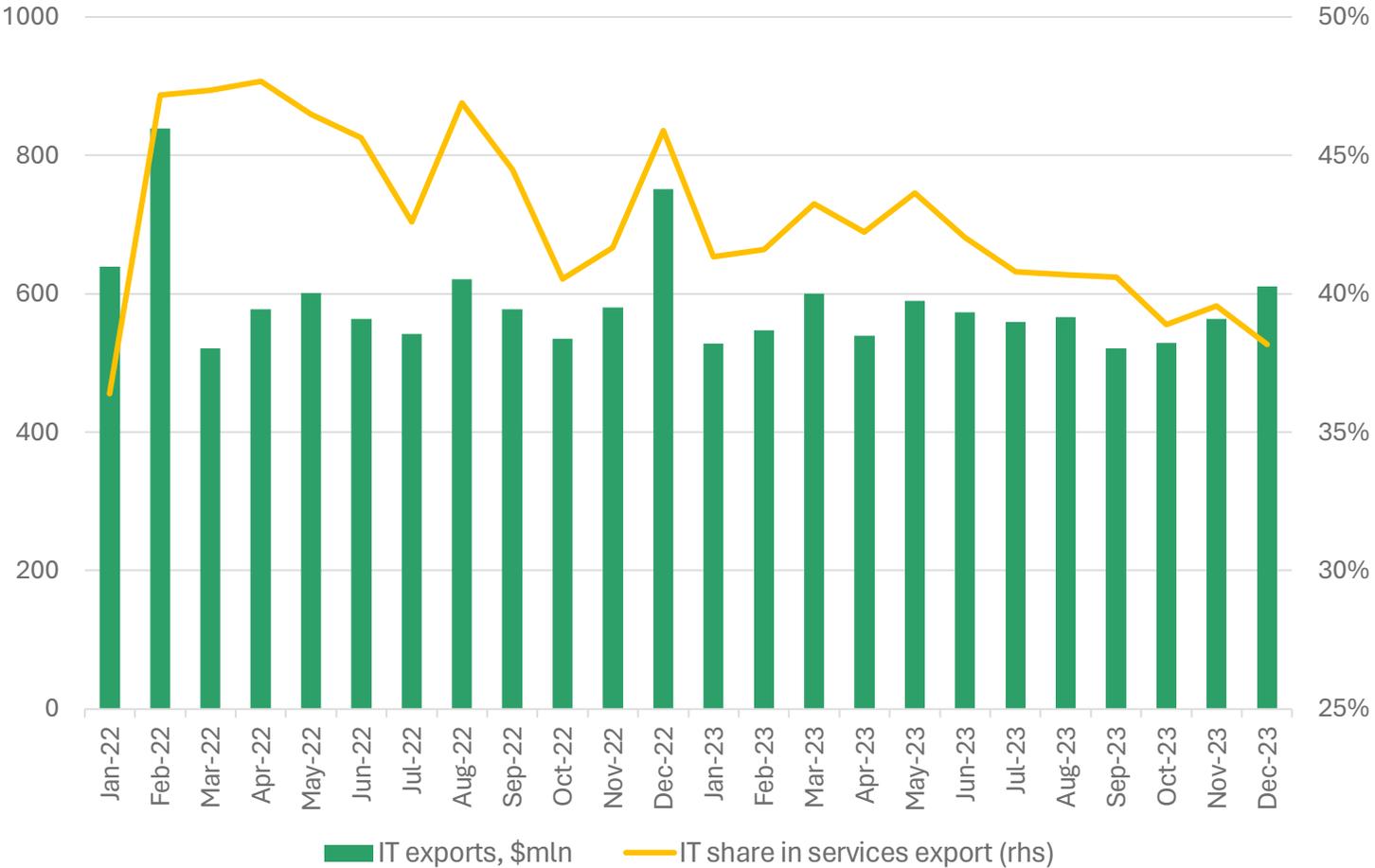


- Total volume of exports of grain and oilseeds in January increased 0.5% m-o-m to 6.02 million tones.
- **Polish farmers continue to protest Ukrainian grain.** Another one began on February 9. Two days later, it escalated when **grain from Ukrainian trucks was forcefully spilled onto the roadway.**
- **Agricultural companies have received 40% of all grants under the eRobota program,** which provides funding for existing and new processing companies. On February 5, the first wave of applications for grants for processing companies under the New Level program was launched. Under this program, entrepreneurs can receive a grant of up to UAH 8 million for business development, and a prerequisite for the grant is that the grantee creates at least 25 new jobs.
- **The first vessel with wheat in 2024, chartered by the UN World Food Programme (*Grain From Ukraine*), has been shipped through the Black Sea.** The volume of grain exported under this program exceeded 195 kt.
- **Russia continues to destroy Ukraine's agricultural infrastructure.** An attack on the night of January 31 destroyed one of the PAEK Group's enterprises in Mykolaiv region, damaging warehouses and equipment, and crops were lost.

Sources: Ministry of Infrastructure, Ministry of Agriculture, State Custom Service, UN, Dragon Capital estimate.

SECTORAL ANALYSIS

IT exports down in 2023 for the first time



- In 2023, Ukraine's IT exports decreased for the first time in the period of observation - by 8.5% to \$6.7 billion.
- The share of IT in service exports in December was 38%, the lowest since the start of the full-scale invasion, and 41% in 2023.
- Despite that market participants negatively assess these current dynamics, the volume of monthly exports of IT services in December increased for the third consecutive month to \$611 million, the highest value in 2023.
- The US accounted for 36% of the export structure.
- In January, the number of vacancies on the market reached its highest level in the last year and a half, thanks to the appearance of 1665 new vacancies on the largest industry job search resource.

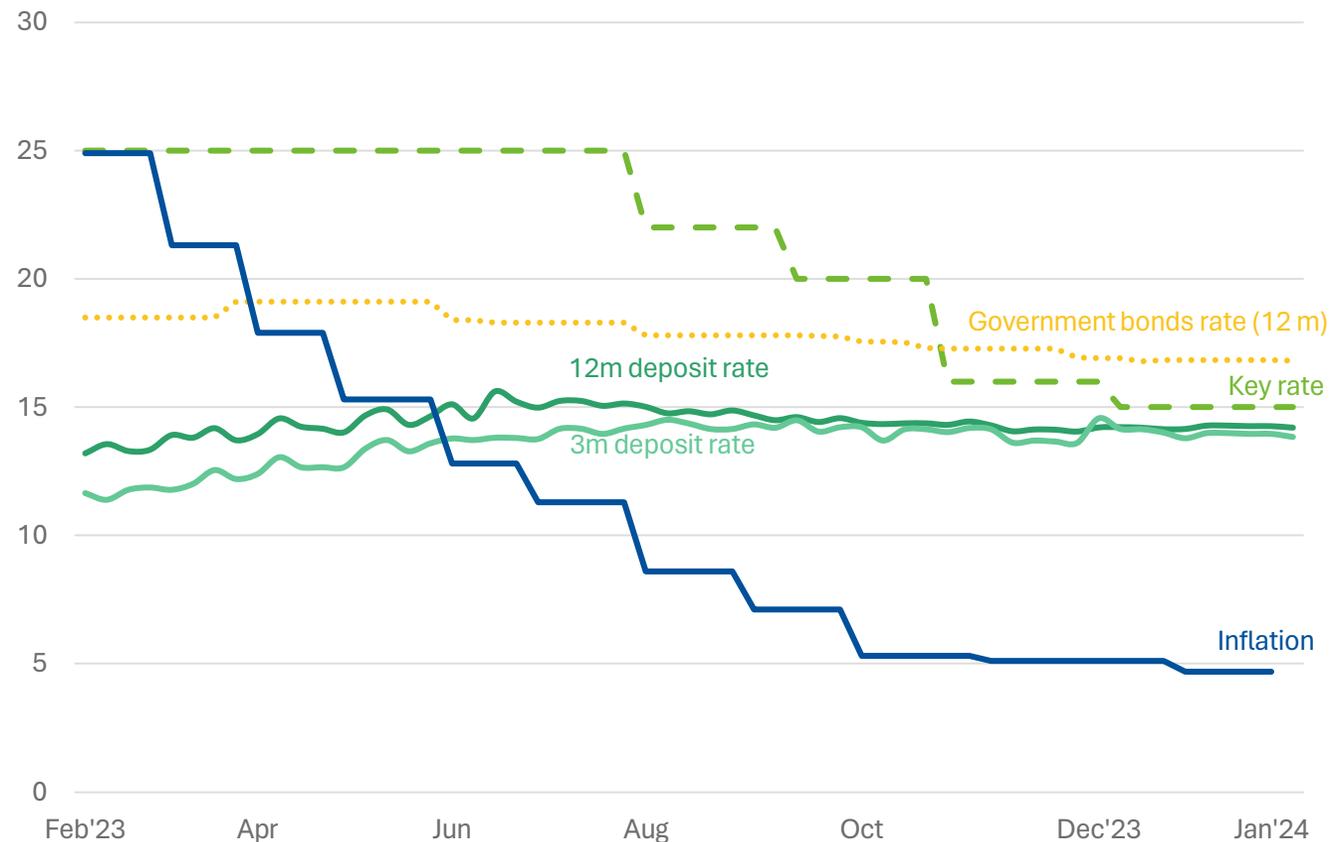
Sources: NBU, CES calculations

MONETARY AND FX SECTOR

MONETARY AND FX POLICY

Key policy rate remained stable – 15%

Inflation (y-o-y), NBU key rate, rates on hryvnia retail deposits (12- and 3-month), and weighted average level of yield on 1-year hryvnia government bonds, %

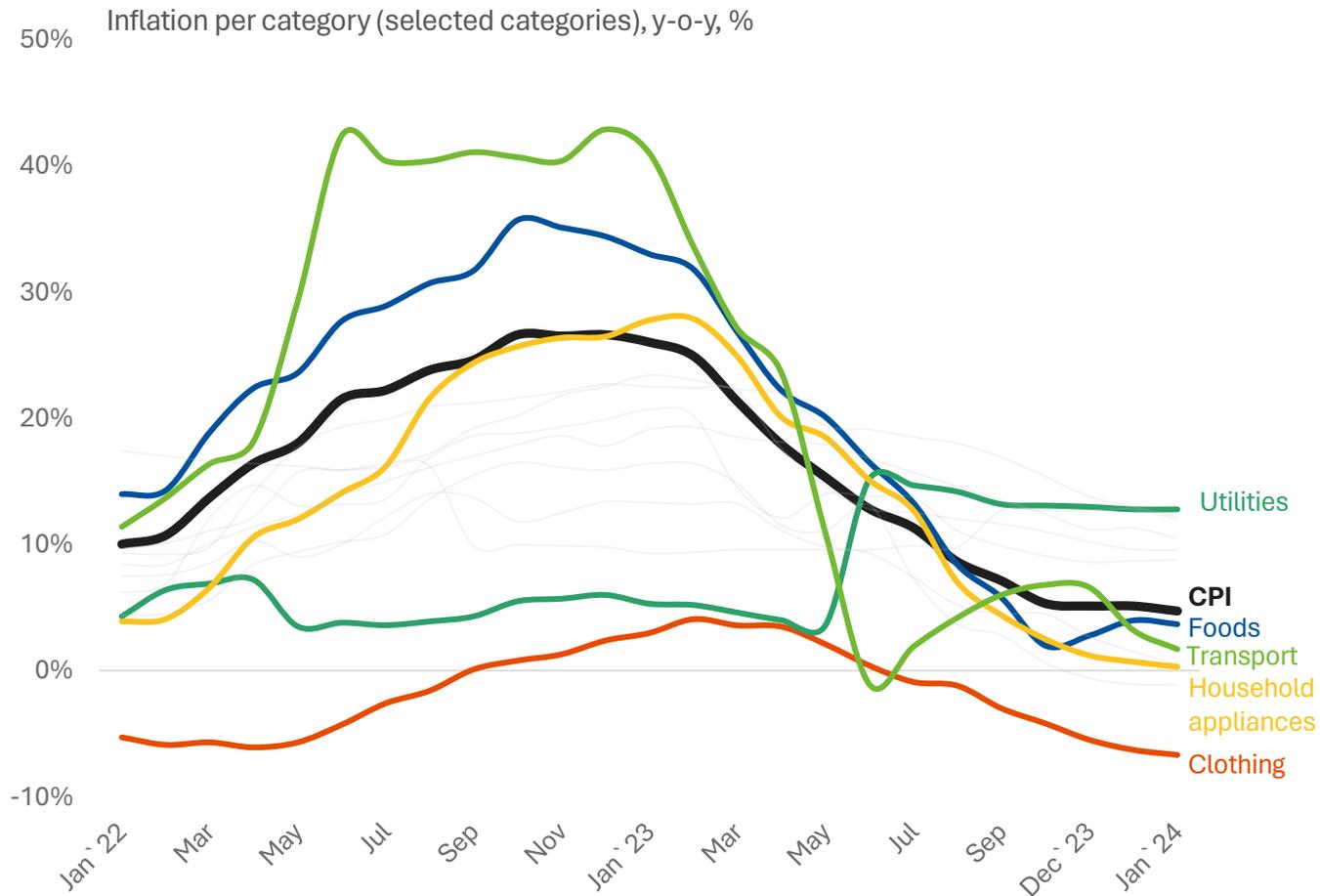


Sources: NBU, State Statistics Service, UIRD

- The key policy rate has remained at 15%.
- The NBU decided not to change it, as there is a need to maintain exchange rate sustainability, keep inflation moderate in 2024, and bring it to the target range of $5\% \pm 1$ p.p. already in 2025.
- A lot of attention will be given to the maintenance of the sufficiently high-interest rates on hryvnia instruments this year.
- There might be a slight reduction in the key policy rate starting from the 2nd half of 2024 if the macroeconomic situation allows, and the rhythm of international aid is restored.
- The yield of one-year hryvnia war bonds and 3- and 12-month deposits have remained at the same level as in December 2023.

MONETARY AND FX POLICY

Inflation slows down; CPI 4.7% y-o-y in January 2024



- In January 2024, inflation was recorded at its lowest level since 2020 – **4.7% y-o-y**.
- Over the past month, prices have fallen the most among food products: eggs (-8.4 %) and sugar (-2.9%), and non-food goods – clothing and footwear (-5.5%) and fuel and lubricants (-4.6%).
- Prices have increased the most among food products: vegetables (+16.8%) and fruits (+4.5%). Among non-food – railway transport (+2.5%) and health care (+1.3%).
- In the first months of 2024, inflation will stay near current levels but will rise to **8.6%** by the **end of the year**, mainly due to the diminishing impact of favorable weather on food supply and increasing business costs.

MONETARY AND FX POLICY

International reserves decreased but stayed sufficient – 5.1 months of import coverage

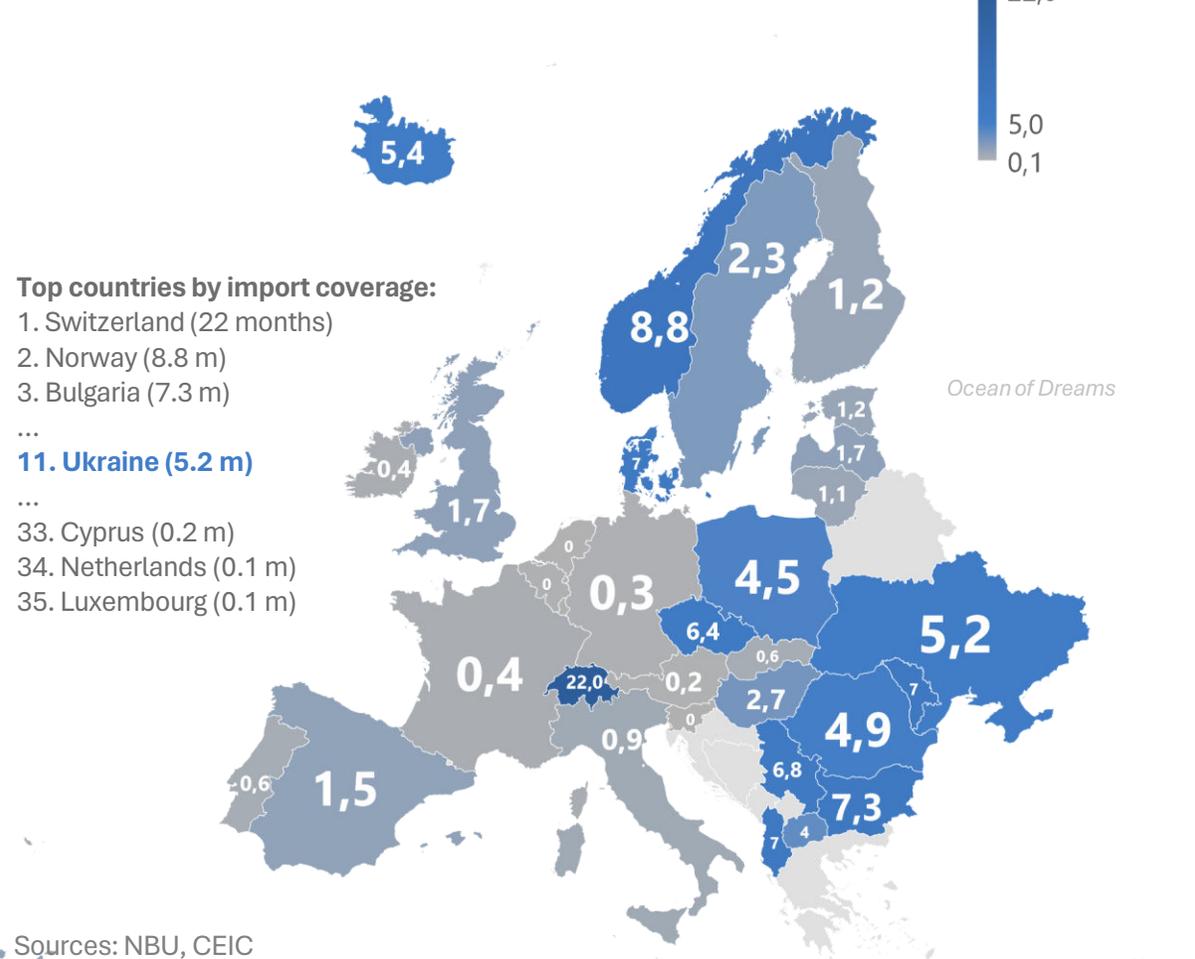
In January, international reserves fell by 5% to over \$38.5 bn (5.1 months of import coverage) due to lower financial aid to Ukraine than in previous months. There is still a need for significant FX sales to replenish reserves, and service and repay the FX public debt.

NBU foreign exchange interventions, USD bn



Source: NBU

Months of import coverage as of Oct 2023*



Sources: NBU, CEIC

* For Latvia and Portugal as of September 2023

Hryvnia revalued after its sudden devaluation in the 1st half of January



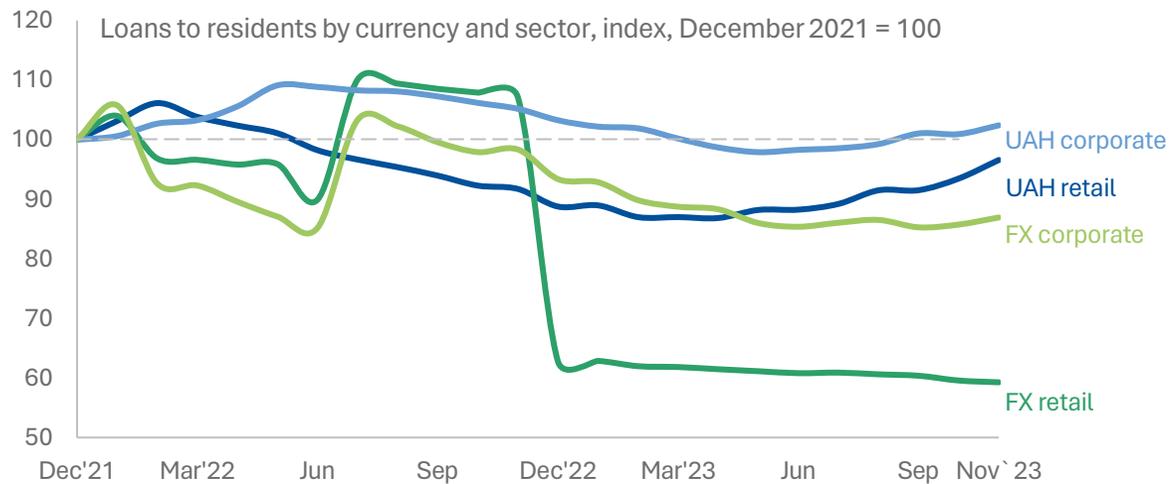
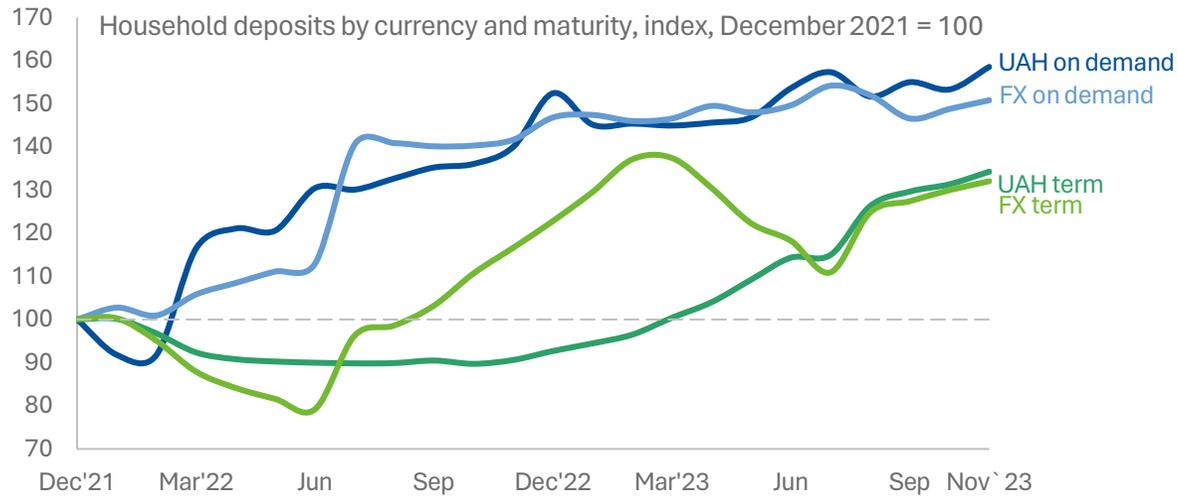
- In January, the cash market hryvnia rate devalued in the first half of the month, reaching 38.5, but then started going down along with the official rate. **The official hryvnia rate reached 38.3 on January 9, a new historic low.**
- For more than four months already, the NBU has been adhering to the managed exchange rate flexibility regime. After the transition to this regime, the volumes of bank operations without the participation of the NBU increased significantly.
- Due to substantial international reserves, the NBU will persist in offsetting the currency shortfall in the market, thus ensuring exchange rate stability.



BANKING SECTOR

BANKING SECTOR

Hryvnia loans and FX-term and Hryvnia deposits are on the rise



Source: NBU

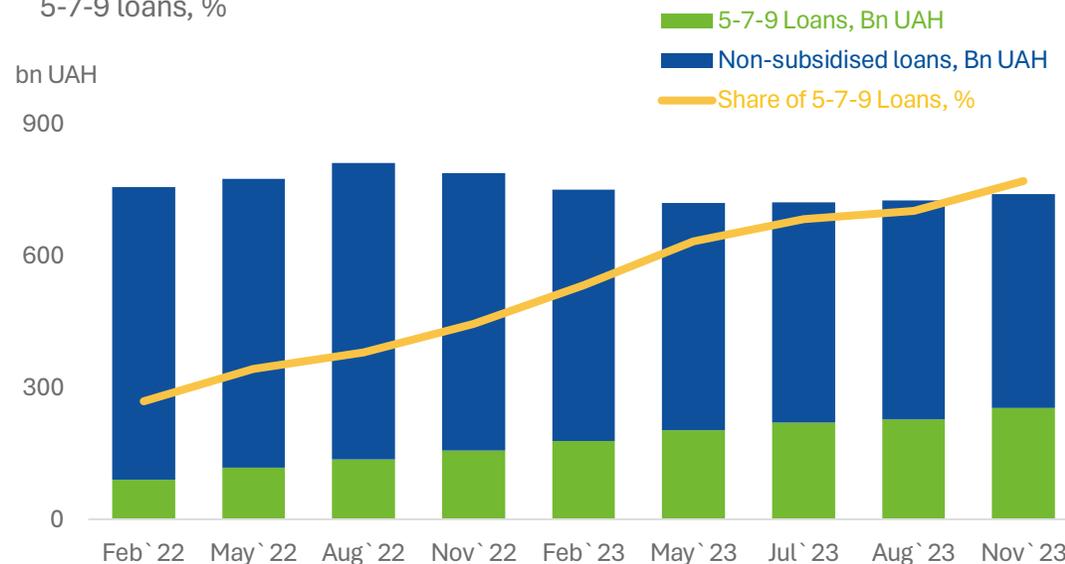
- By the end of 2023, there was a continued growth trend in the amount of funds held by clients. **The deposits of households were growing faster than those of businesses.**
- Financial institutions expect **a decrease in borrowing costs from both businesses and households in Q1 2024**, but funding volume will remain stable.
- In 2023, demand for loans increased, **especially for foreign currency and large companies**. For the first time in 5 quarters, **large businesses requested more loans than SMEs**. Lower interest rates and the need for working capital and investment drove the demand.
- Based on the Bank Lending Survey, in January-March 2024, **banks are anticipating a rise in the demand for business loans**. The majority of these loans are **for hryvnia and short-term purposes**, including those for large companies.

BANKING SECTOR

Affordable Loans 5-7-9% program

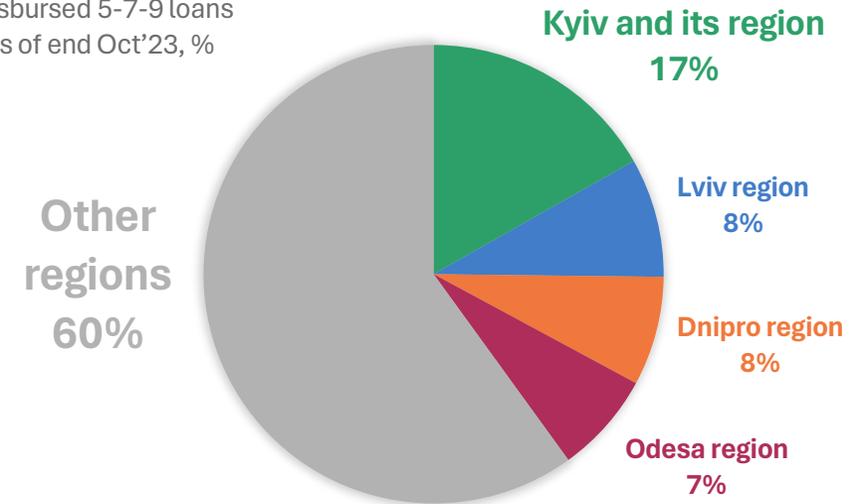
- Most of the lending occurs under the Affordable Loans 5–7–9% program. Loans granted within this program comprise 1/3 of the hryvnia corporate loans.
- The primary users are businesses within **agriculture (49%)**, **wholesale (26%)**, and **industry (15%)**, while most of the loans are disbursed in **Kyiv city and its region (17%)**.

Subsidized and non-subsidized corporate loans, bn UAH, and share of 5-7-9 loans, %

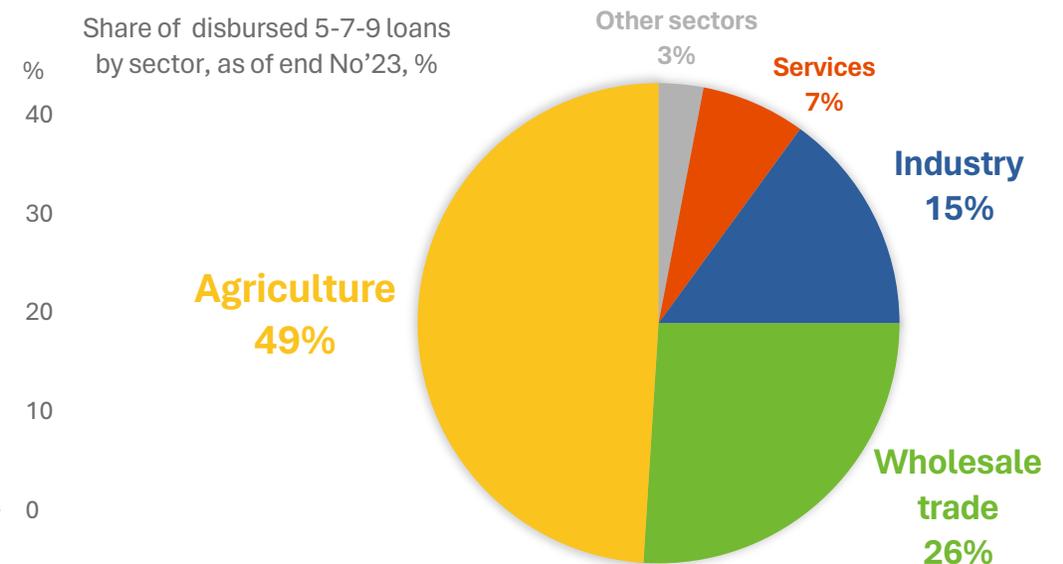


Source: NBU, BDF

Share of disbursed 5-7-9 loans by region, as of end Oct'23, %



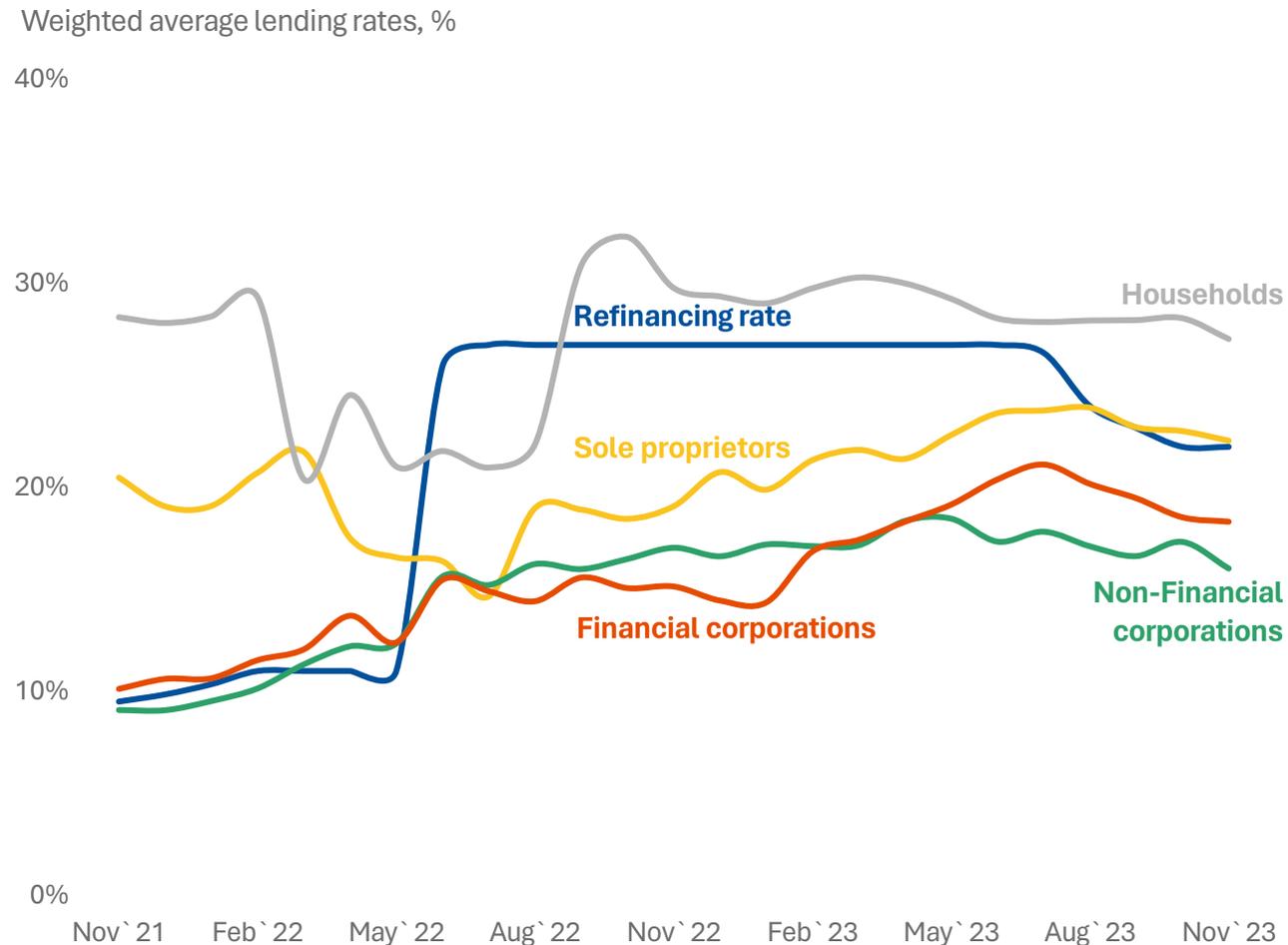
Share of disbursed 5-7-9 loans by sector, as of end No'23, %



Source: BDF

BANKING SECTOR

Lending rates demonstrate downward trend

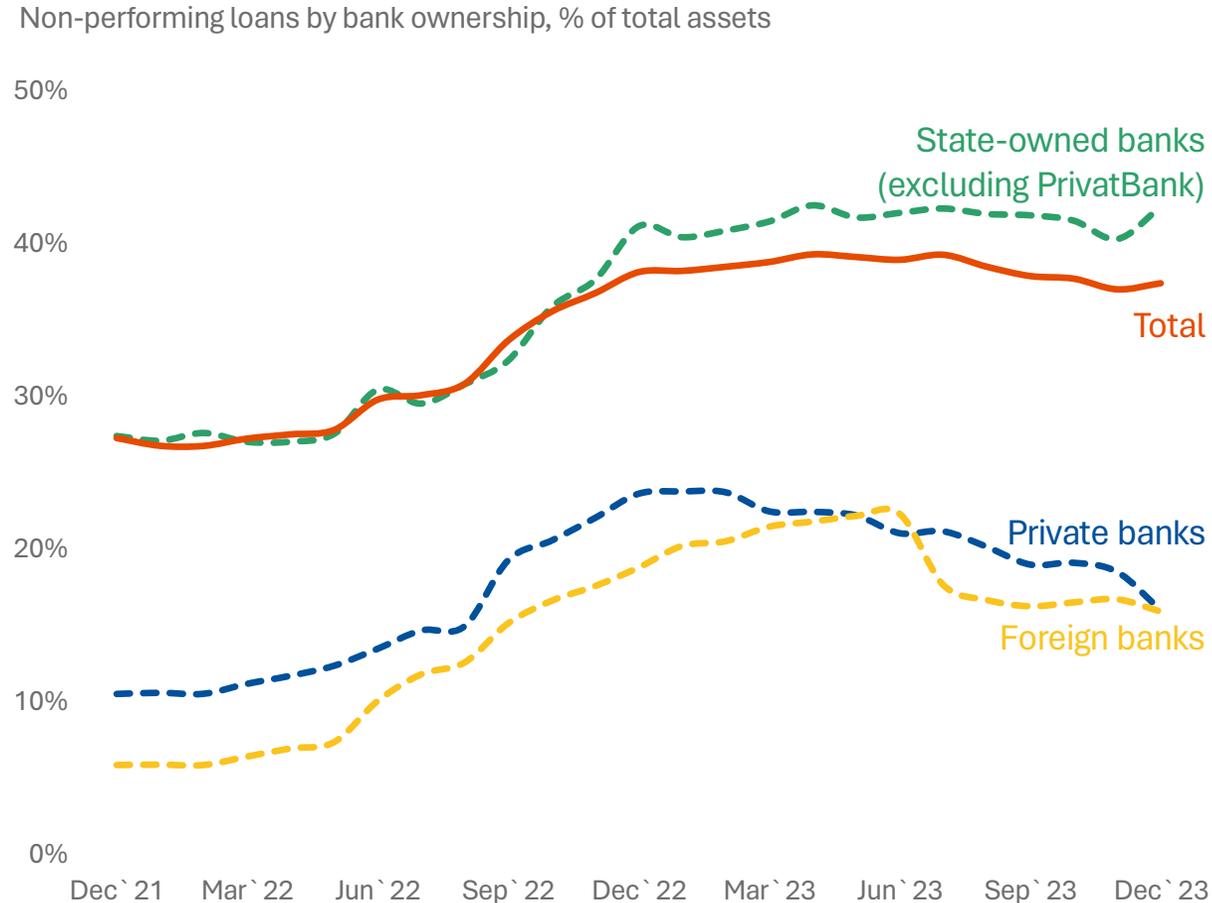


Source: NBU, monthly average

- Based on the NBU`s modernized operational design of its monetary policy, **the refinancing rate = the key policy rate + 6 p.p.**
- The softening of the key policy rate contributed to **cheaper lending**, resulting in a **decrease in the weighted average interest rates on hryvnia loans for NFC**, down to 16% in Nov`23.
- Lowering rates for non-subsidized loans has a positive effect on lending volumes and helps to restore client-bank market relations.
- Although **interest rates on hryvnia loans to individuals** also decreased, they **remained significantly higher than loans to enterprises** due to the high proportion of unsecured and high-risk loans.
- Gradually, bank lending has been restored as a result.

BANKING SECTOR

Non-performing loans (NPLs) ratio slightly decreased to 37.4% during 2023

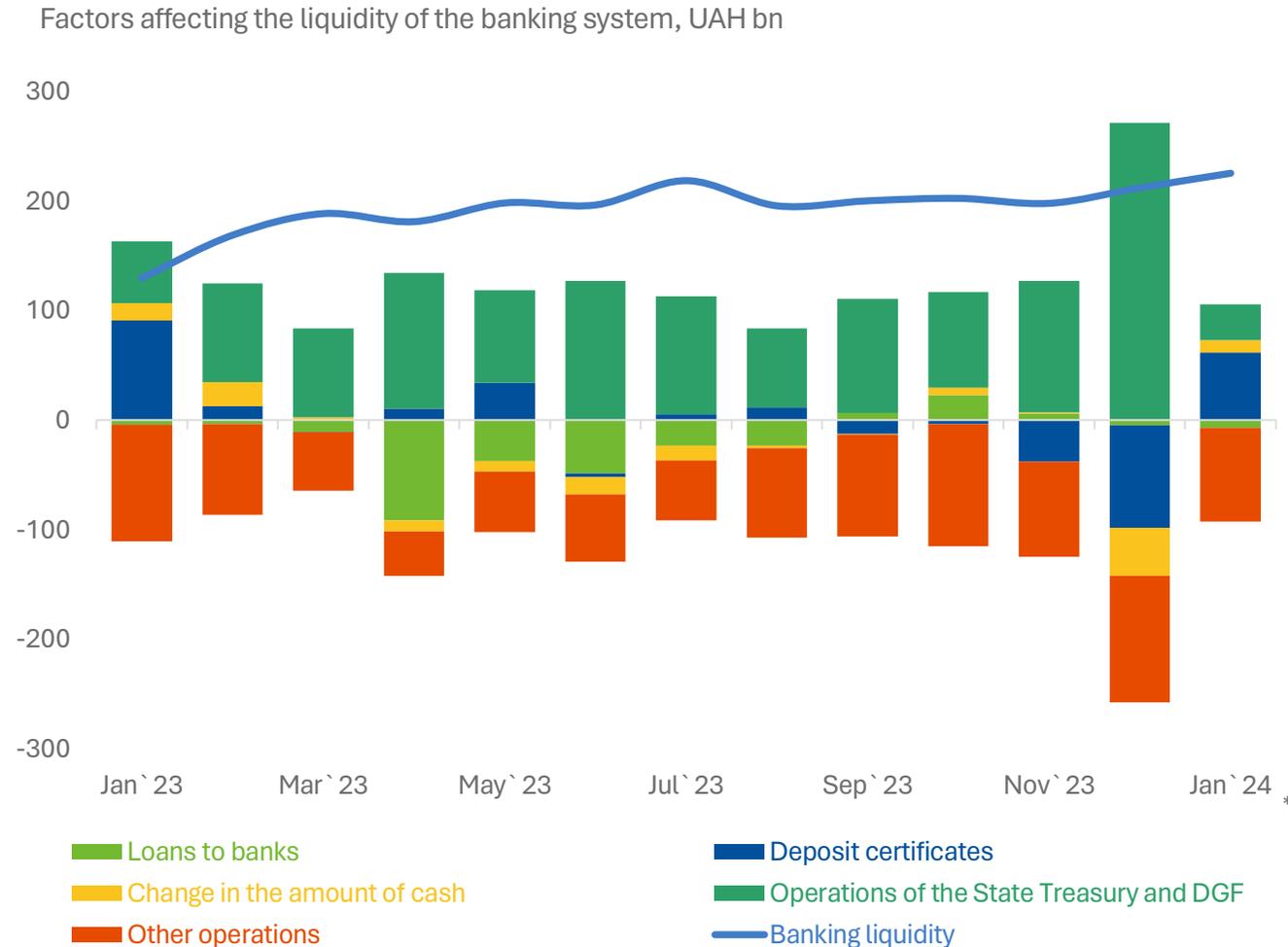


Source: NBU

- By January 1, 2024, the banking sector had UAH 422.4 billion in NPLs, down UAH 9.7 billion from January 2023. The NPL ratio decreased to **37.4%** over this period (-0.4 p.p.).
- The main factor that contributes to reducing the share of NPLs is **the growth of the loan portfolio**. Despite the ongoing war, lending has continued.
- Other reasons for the decrease in NPLs include **corporate debt restructuring, improved debt servicing, and write-offs of non-performing loans to individuals**.
- Banks restructured **over 89% of non-performing "military" loans**, amounting to UAH 73 bn. Over 77% of loans for debtors with lost or occupied assets are reserved.

BANKING SECTOR

Banking liquidity on its highest level



- Between December 2023 and January 2024, the liquidity of the banking system started to grow again after a period of calm in the second half of summer and fall, **reaching its highest value of UAH 226 billion.**
- The increase in liquidity was mainly due to the **government's significant rise in spending**, which went beyond the interventions made by the NBU, and the **seasonal increase in cash flow** towards the end of the year.
- In 2024, we can expect **liquidity to rise again** due to the government's planned high spending.
- However, as the budget deficit financing decreases with the help of international aid in the future, the liquidity of the banking system will gradually decrease. Nonetheless, **it is still expected to remain significant.**



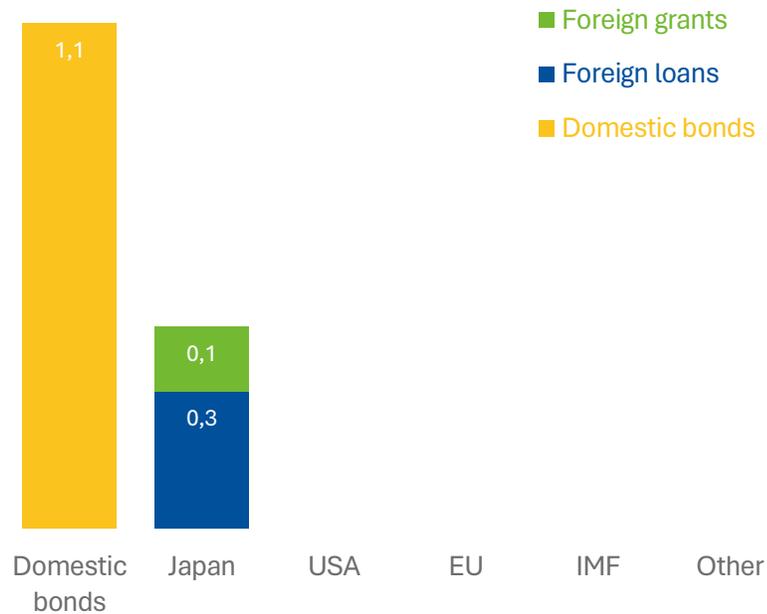
FISCAL SECTOR

FISCAL SECTOR

Only \$0.4 bn of foreign financing in January

In January, Ukraine received just \$0.4 bn of foreign financing from Japan — the lowest amount since the beginning of the full-scale war.

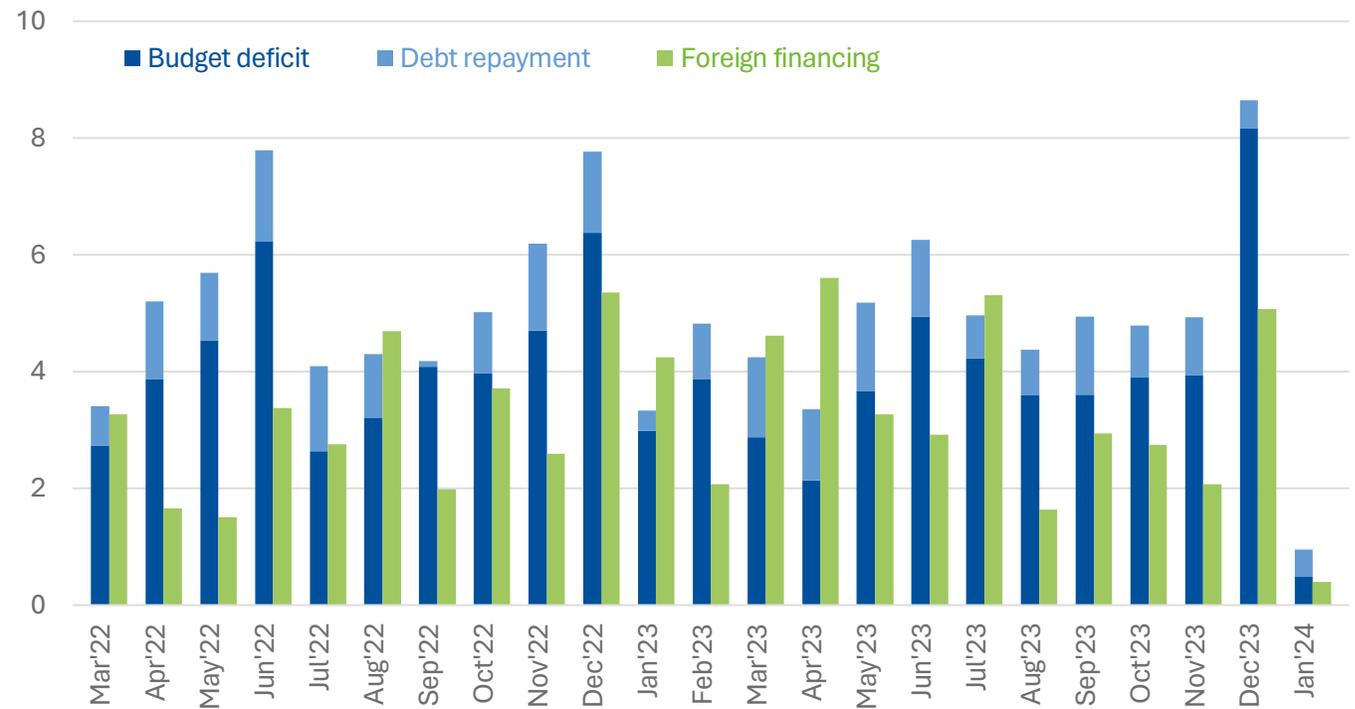
2024 additional financing of Ukraine's state budget as of February 7, \$bn



Source: Ministry of Finance

Ukraine drastically reduced its state budget deficit in January to survive the month with reduced foreign financing. It was done mostly by postponing budget expenditures, together with strong, but one-off tax revenues.

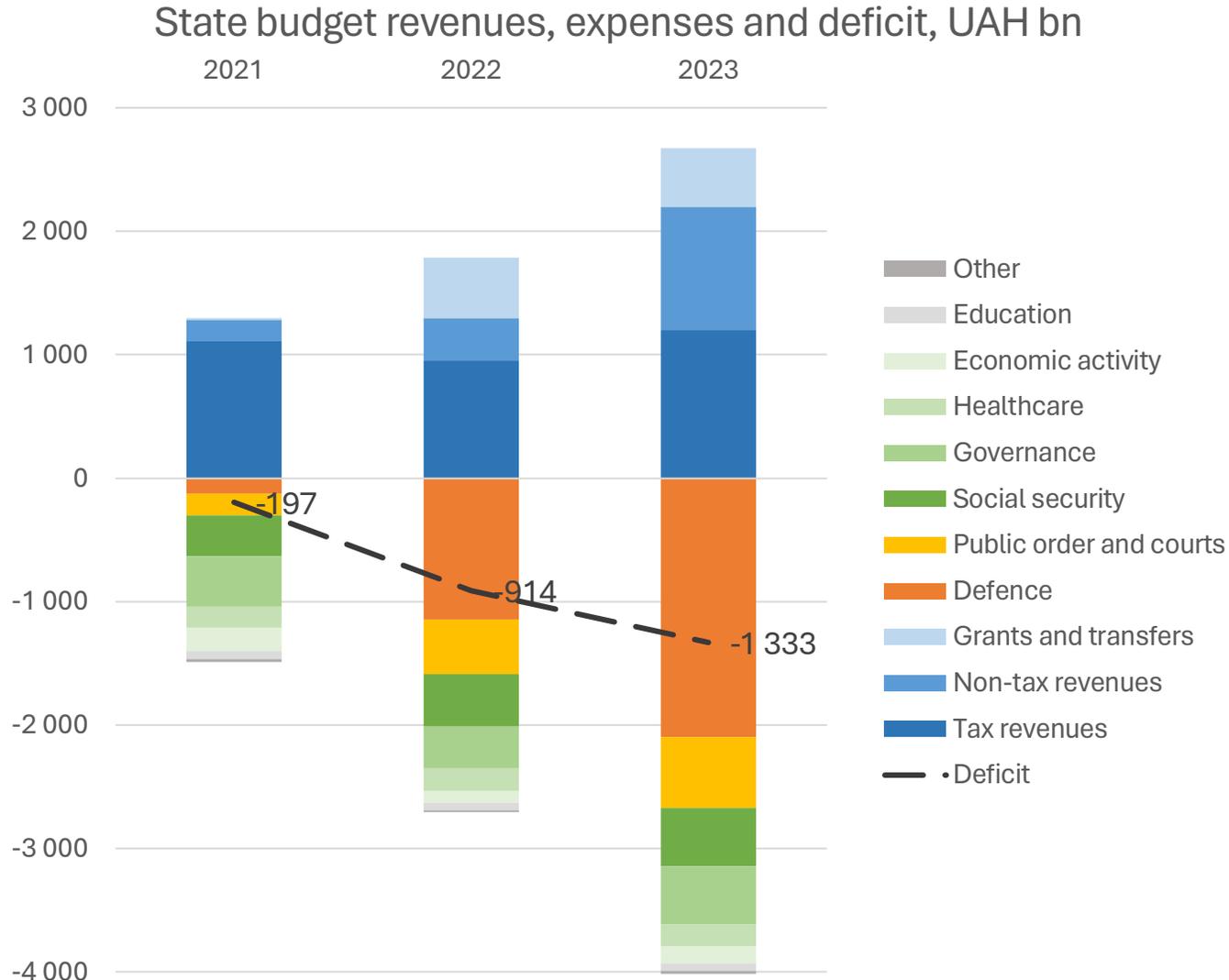
Foreign financing, state budget deficit and debt repayment, \$bn



Source: Ministry of Finance, NBU, CES calculations

FISCAL SECTOR

Budget deficit in 2023 expanded despite rebound in tax revenues



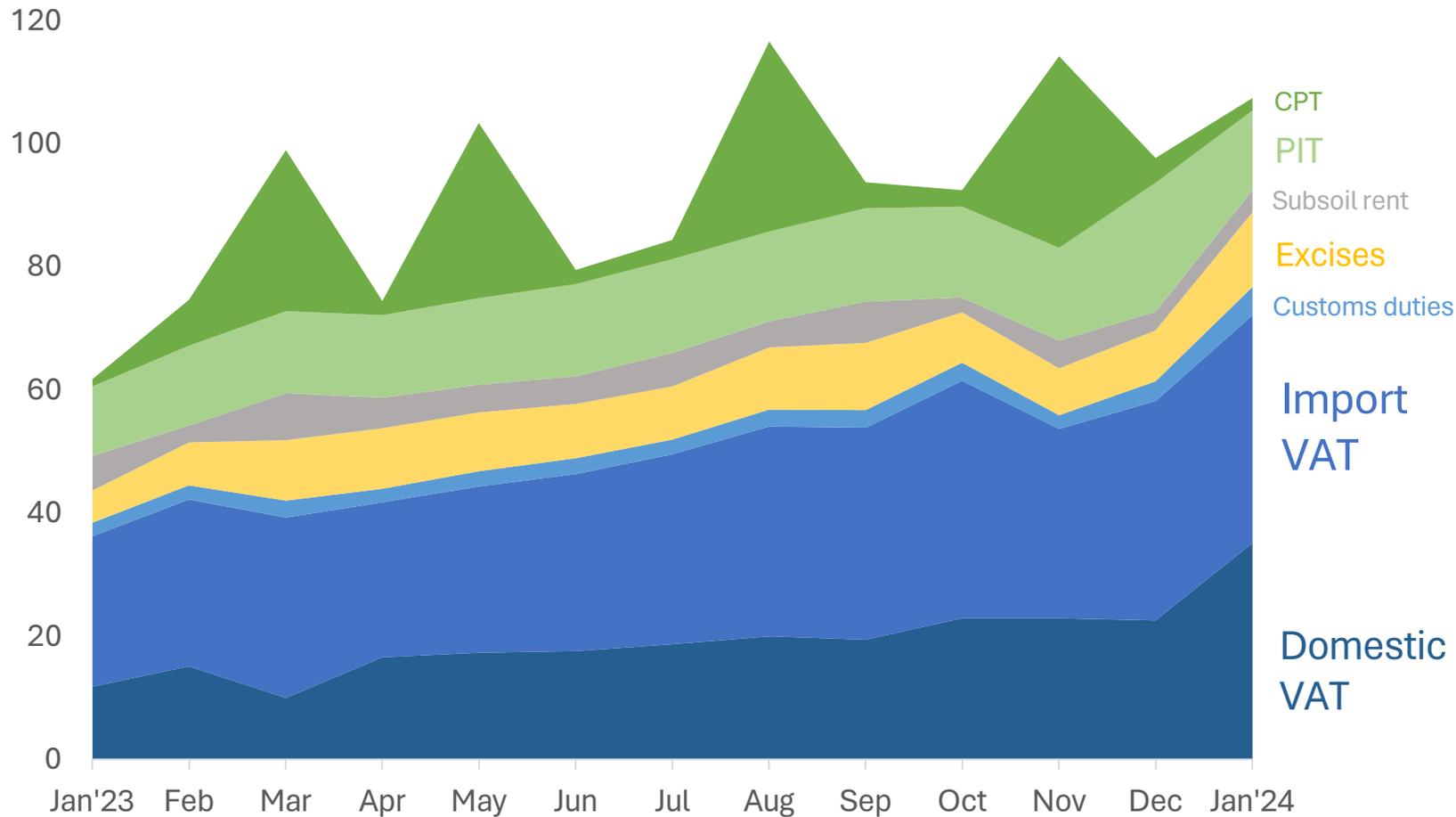
Budget deficit in 2023 expanded further, driven by war expenditures, with **52% spent on defence (84% increase YoY)** and another 14% - on public order and security.

Non-tax revenues reached 37% of state budget revenues (UAH 991 bn vs UAH 1 203 bn of tax revenues).

More than $\frac{3}{4}$ of these non-tax revenues are the own revenues of budget entities, most of which are **accounted military aid** by nature.

FISCAL SECTOR – TAX REVENUES

Revenue hike in Jan driven by one-offs



Source: Ministry of Finance

Tax revenues of state budget in January were UAH 107.4 bn

Taxes from consumption hiked driven primarily by net domestic VAT revenues (UAH 35.1 bn vs UAH 22.5 bn in December) due to:

- doubled defence spending in December (+160 UAH bn), part of which were advances to local business;
- decreased VAT credit due to delays at customs in Dec (“blockade” at UA/PL border);
- strong domestic consumption pre-holidays.

Note: the detailed breakdown by sources is not available as only preliminary June figures were released as of the current date



THANK YOU.

This text reflects the opinion of the authors and does not necessarily represent the views of the German Economic Team.