CENTRE FOR ECONOMIC STRATEGY

GET German Economic Team

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Author: CES Team

Economy review in June

Special topic: What prevents Ukrainian businesses from raising funds?

EXECUTIVE SUMMARY

EXECUTIVE SUMMARY: UKRAINIAN ECONOMY IN JUNE 2024

CENTRE FOR ECONOMIC STRATEGY

- **Macroeconomic trends:** Real GDP in the first quarter of 2024 increased by 6.5% y-o-y; the economic recovery will slow down in the next quarters of the year. Business expectations fell in June due to the deteriorating security situation, significant power outages, and rising production costs.

- **Sectoral analysis:** Ukraine doubles electricity imports for the second month in a row as the electricity crisis worsens. Steel production remains at local highs on higher iron ore exports. Agri exports at 70 mln t - 2023/2024 marketing year results.

- **Monetary, FX, and Banking sector:** Inflation accelerates– 3.3%, and key rate policy remains stable - 13%. Hryvnia continues to devaluate, setting a record – 40.8 UAH/$; the international reserves decreased but remain sufficient; lending continues to grow moderately, including non-subsidised loans.

- **Fiscal sector:** Ukraine received $2 bn of foreign budget assistance in June. Tax revenues have shown a strong growth y-o-y in the first half of 2024 but have been stagnating since April. State budget expenses in May increased by 29% to UAH 390 bn, with defence spending growth of 34% m-o-m, to UAH 206 bn.

- **Special topic:** Despite the large number of options for attracting funds from banks, financial institutions, the government, and international partners, it is not always easy for Ukrainian businesses to borrow money. We examine the main problems and give recommendations to all categories of market participants.

See our report below for further details.

MACROECONOMIC TRENDS

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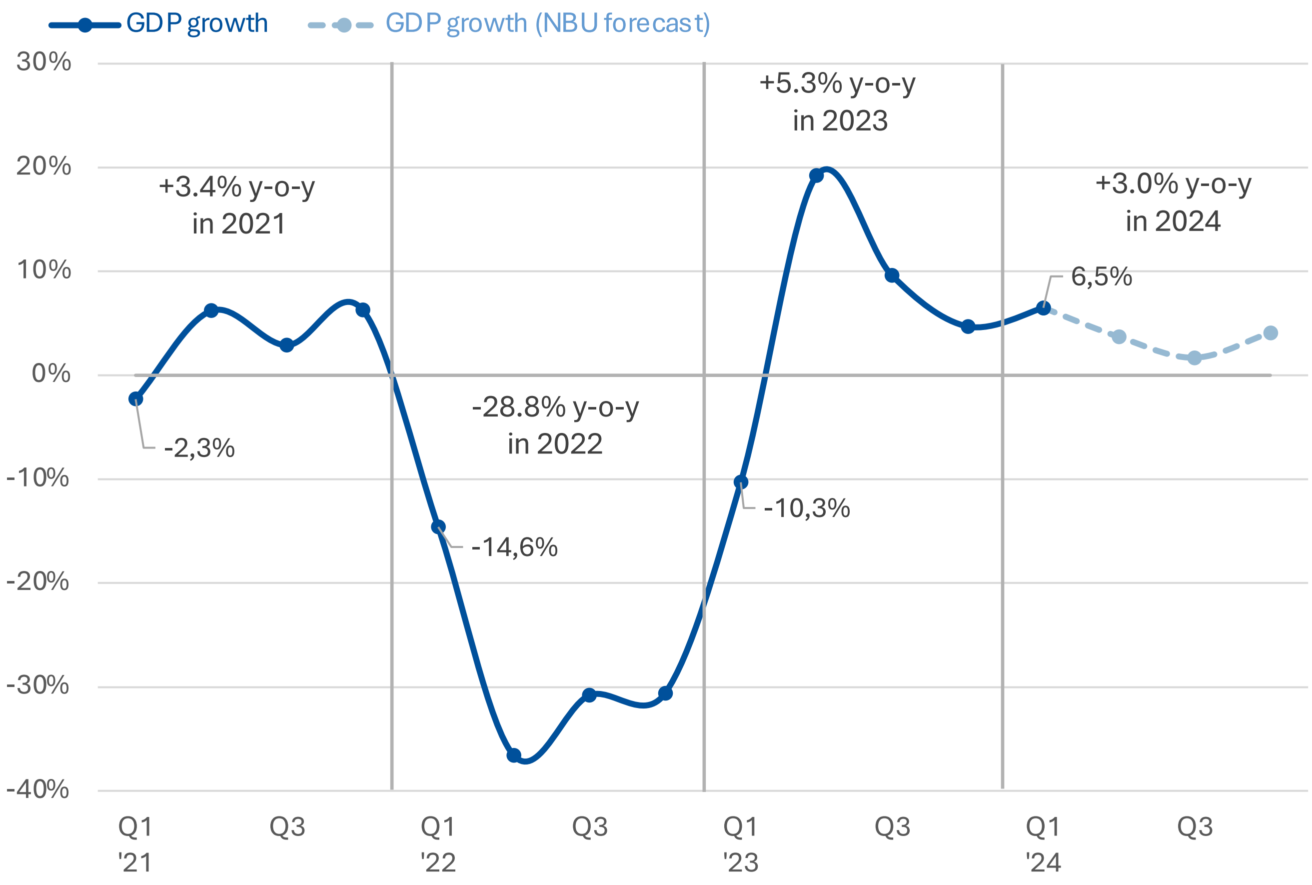
GDP increased by 6.5% in Q1 2024: official data

GDP growth (y-o-y) per quarter, %



Source: State Statistics Service of Ukraine, NBU

- Real GDP in the first quarter of 2024 increased by 6.5% compared to the first quarter of 2023, according to the State Statistics Service of Ukraine estimation.
- The economic recovery will slow down in the next quarters of the year.
- According to the forecast of the Ministry of Economy, GDP will grow by 3.5% y-o-y this year (the NBU forecast is 3%).
- These forecasts are in line with the IMF's baseline scenario. However, under the negative scenario, the IMF predicts a 1.7% contraction of the Ukrainian economy in 2024.

MACROECONOMIC TRENDS

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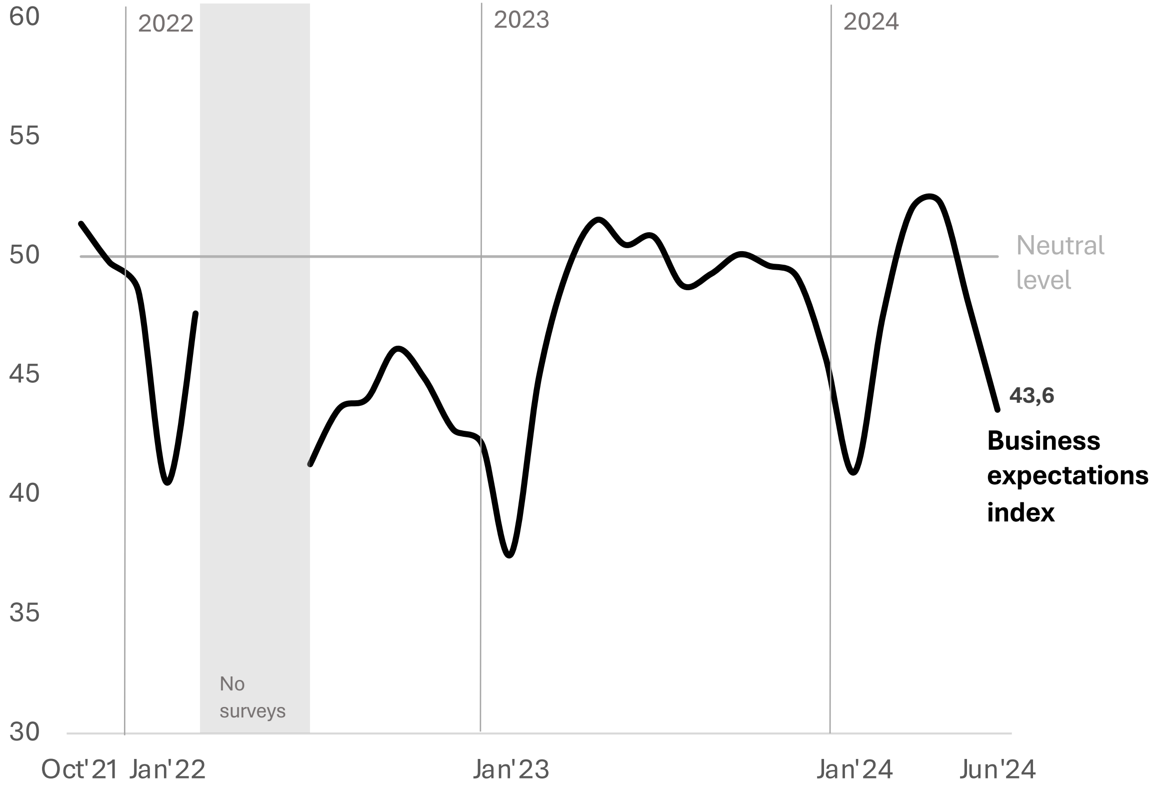
Business expectations fell in June

- **In June, the NBU's business activity expectations index fell to 43.6**, down from 48 in May, and remained below the "neutral" level of 50 points.

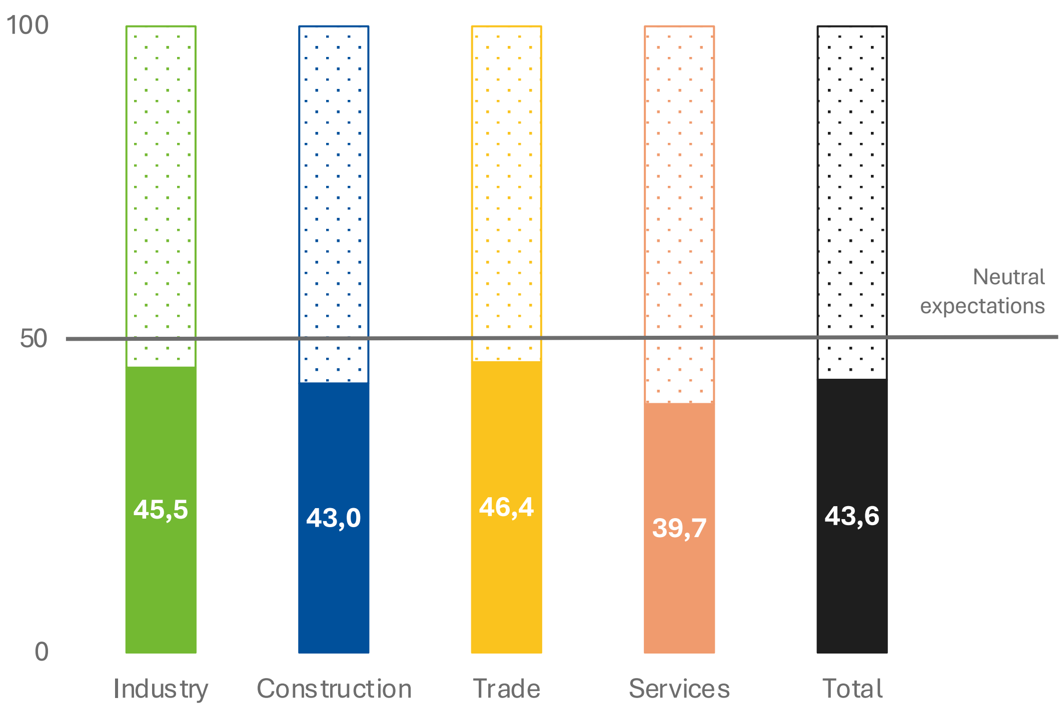
NBU business activity expectations index dynamics



Source: NBU

- **Negative expectations prevailed among businesses in all sectors surveyed.** The mood has deteriorated due to the deteriorating security situation, significant power outages, and rising production costs.

NBU business activity expectations index by sector in June



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SECTORAL ANALYSIS

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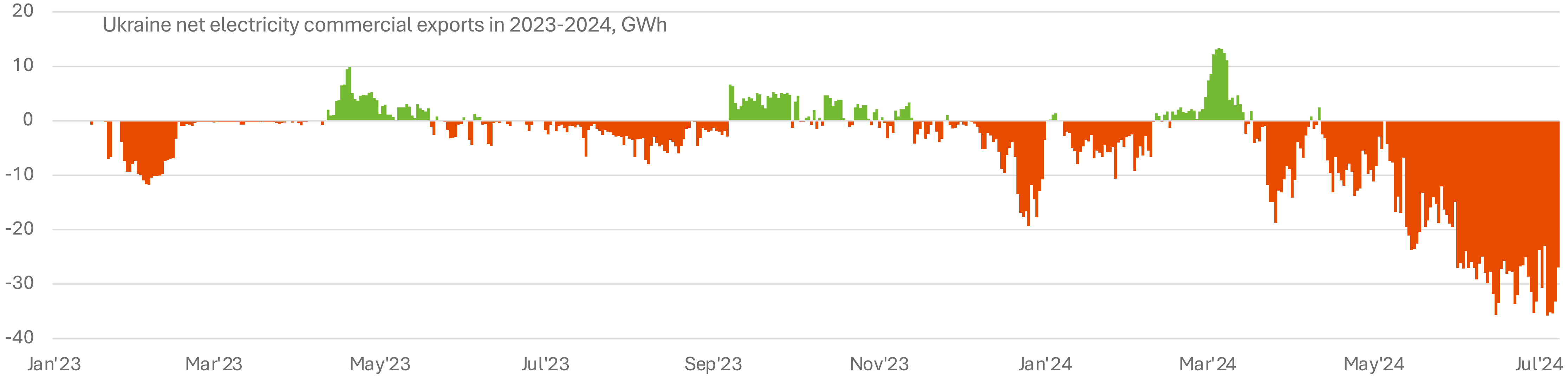
Ukraine doubles electricity imports for the second month in a row

- Hot weather traditionally increases electricity consumption. In June, Ukraine imported 856 GWh of electricity, which is 1.9 times more than in May, which also almost doubled previous wartime import record.
- The last day when Ukraine carried out at least some commercial exports was May 13. The last day when net exports were recorded was April 11.
- Schedules of power outages for residential and industrial consumers continue to be in effect in Ukraine. The planned period of power outages, particularly in Kyiv and Dnipro, exceeds 40%.
- Russia continues to strike at Ukraine's energy infrastructure. The most massive attacks of the summer occurred on June 1 and 20.
- The middle of July is expected to be very hot in Ukraine with temperatures exceeding 35 degrees, which will put additional strain on the country's energy system.



Source: ENTSO-E

SECTORAL ANALYSIS

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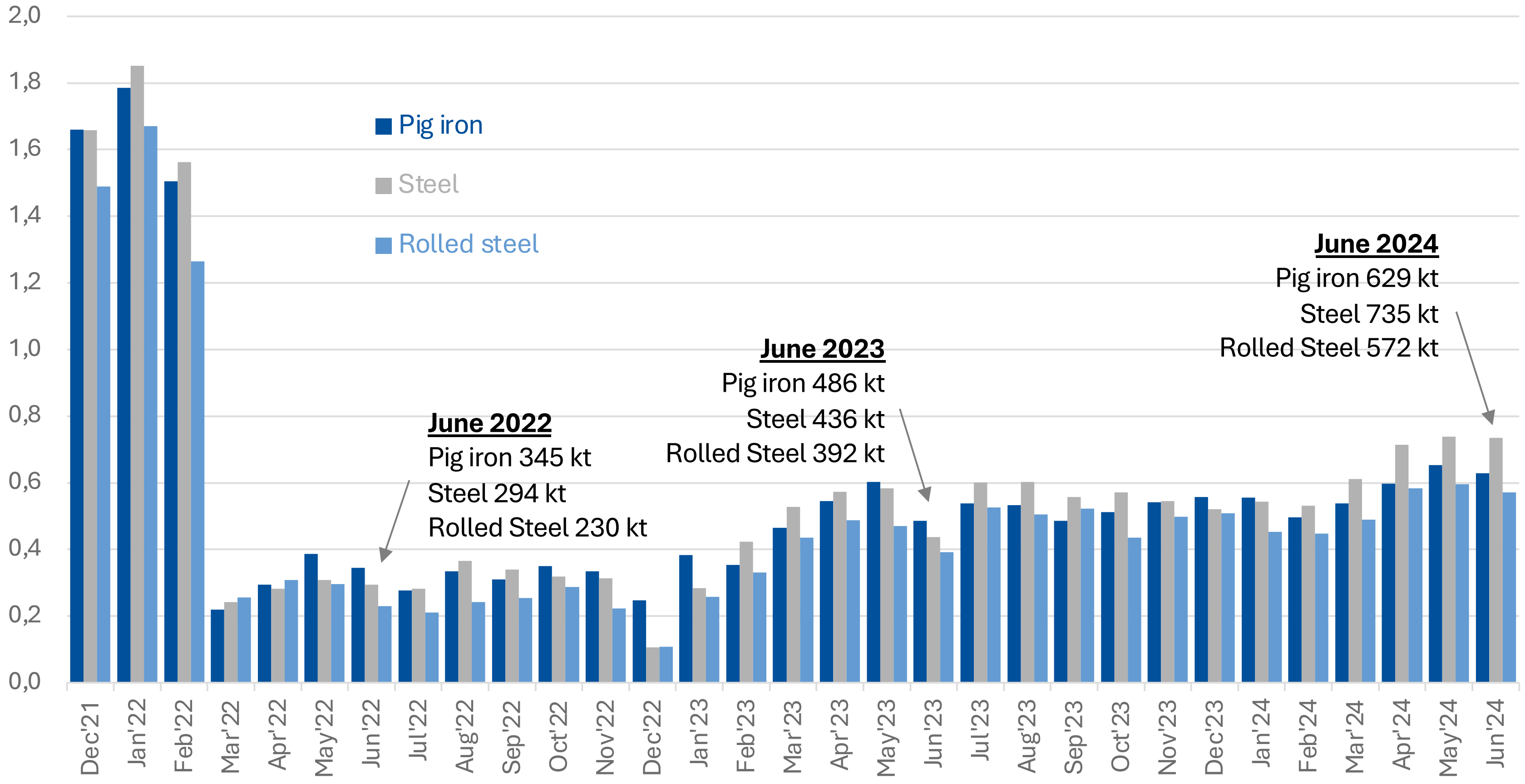
Steel production remains at local highs on higher iron ore exports

Ukraine ferrous production by main categories, mt



Source: Ukrmetalurgprom

- In June, **steel production** remained almost at the level of the previous month (-0.4%) and **amounted to 735 kt**. Pig iron and rolled steel production decreased by 4% to 629 kt and 572 kt, respectively.
- **In 1H2024 steel production increased by 37% to 3.87 mt**, pig iron production by 22% to 3.47 mt, and rolled products by 32% to 3.14 mt.
- In May, **Ukraine exported 3.3 mt of iron ore**. This is -8% m-o-m but 2.06 times more than in June 2023. In total, in January-May, 15.5 mt of ore were exported (up 2.3 times y-o-y) for $1.37 bn (+82%). The main importers were China, Slovakia and Poland. Ukraine's share in EU iron ore imports reached 21%.
- **Domestic consumption** of steel products in 5m2024 **decreased by 4% to 1.36 mt**.
- **Interpipe** presented a major investment project to **expand green steel production capacity worth $1 bn**. It involves the construction of the second stage at the Interpipe Steel electric steelmaking complex and a green flat steel production shop.

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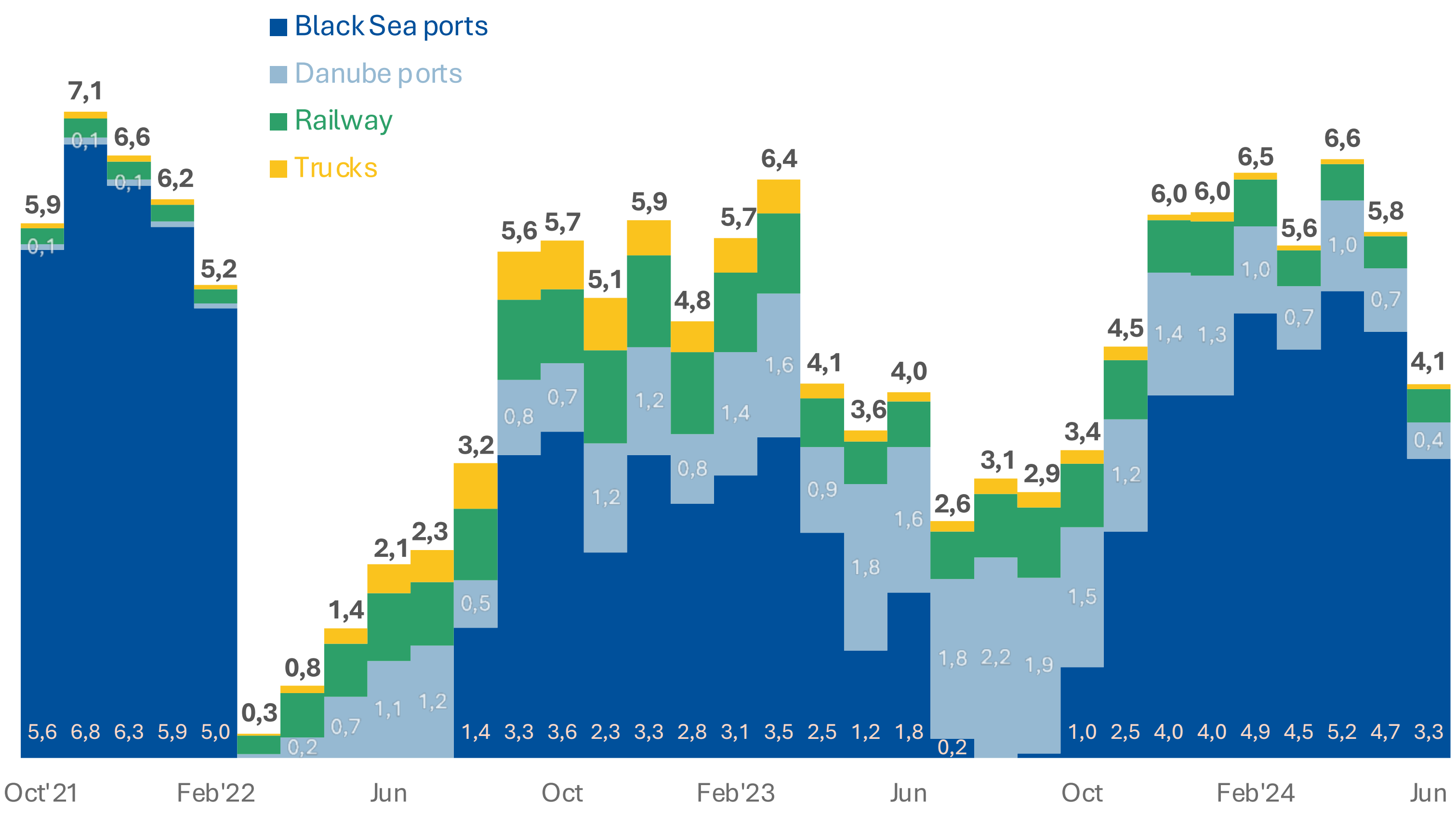
Agri exports at 70 mln t - 2023/2024 marketing year results

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



- Exports of agricultural products in June were down 29% m-o-m as sales of the previous year's harvest were completed. **Compared to June 2023, exports grew by 2%.**
- **In 2023/2024 MY, Ukraine exported 69.86 mt of grain, oilseeds and vegetable oils**. Wheat exports amounted to 18.43 mt (+9% y-o-y). Corn exports amounted to 29.41 mt (+0.2% y-o-y), barley – 2.48 mt (-8.5% y-o-y), soybeans – 2.98 mt (-8.2% y-o-y), rapeseed – 3.7 mt (+8.7% y-o-y), sunflower oil – 6.54 mt (+22.8%), soybean cake – 0.66 mt (+12.5%), sunflower cake – 5.15 mt (+29.1%).
- Last marketing year, Ukraine **exported only 324 kt of sunflower (-86.3% y-o-y)**. This was due to the resumption of sunflower processing in Ukraine.

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

SECTORAL ANALYSIS

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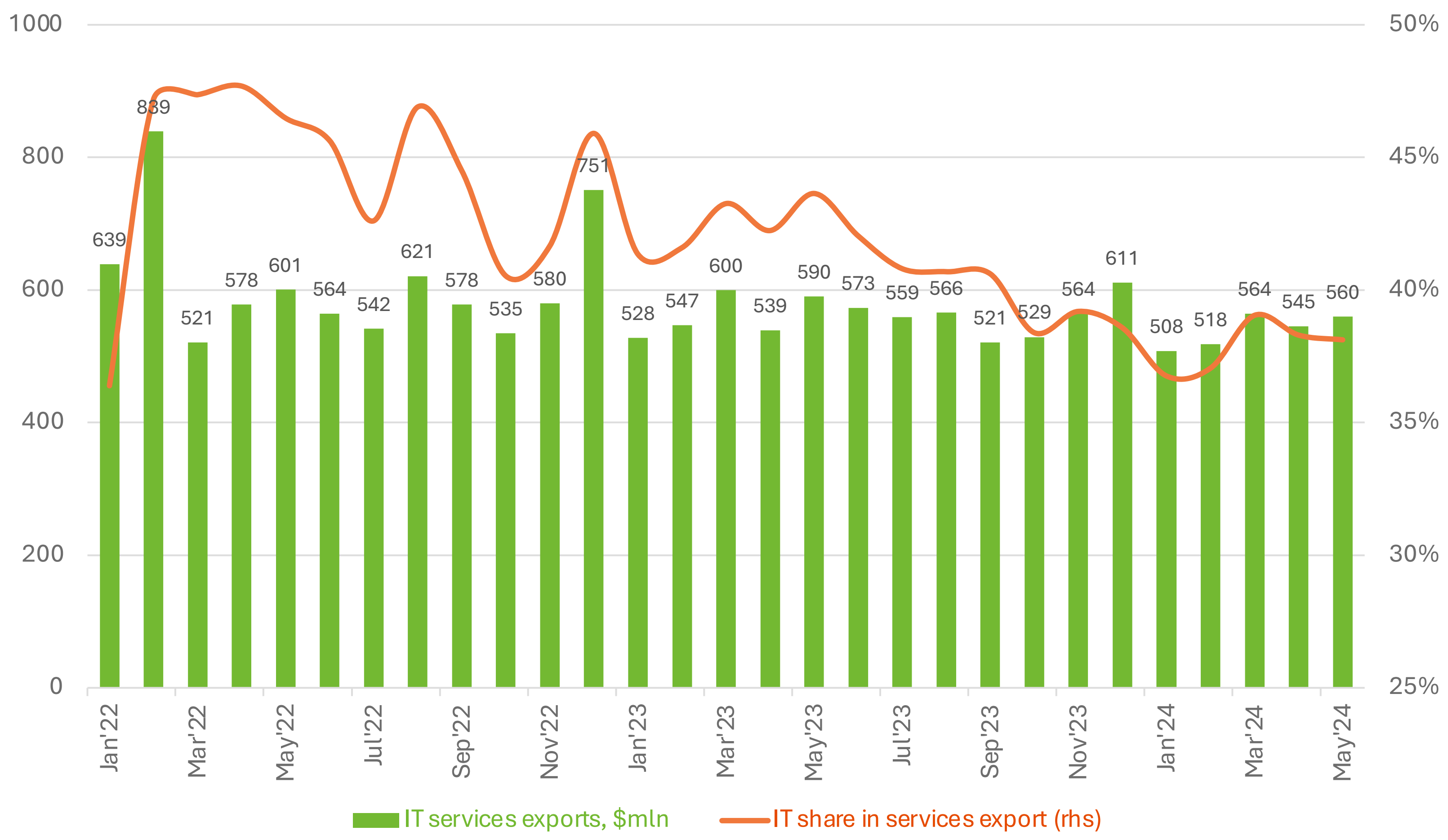
Monthly IT exports have found a balance slightly above $0.5 bn



Sources: NBU, CES calculations

- Exports of IT services in May increased by 3% to $560 mln.
- IT services retain leadership in service exports with a share of 38%.
- In July, the Ministry of Digital Transformation launched beta testing of e-booking in Diia. It is expected to last for several weeks, followed by a public release of the online service, according to Minister Mykhailo Fedorov.
- Even under an optimistic scenario, exports are expected to decrease by 3-5% to $6.4-6.5 bn in 2024,- Lviv IT Cluster estimates.

MONETARY, FX AND BANKING SECTORS

MONETARY AND FX SECTOR

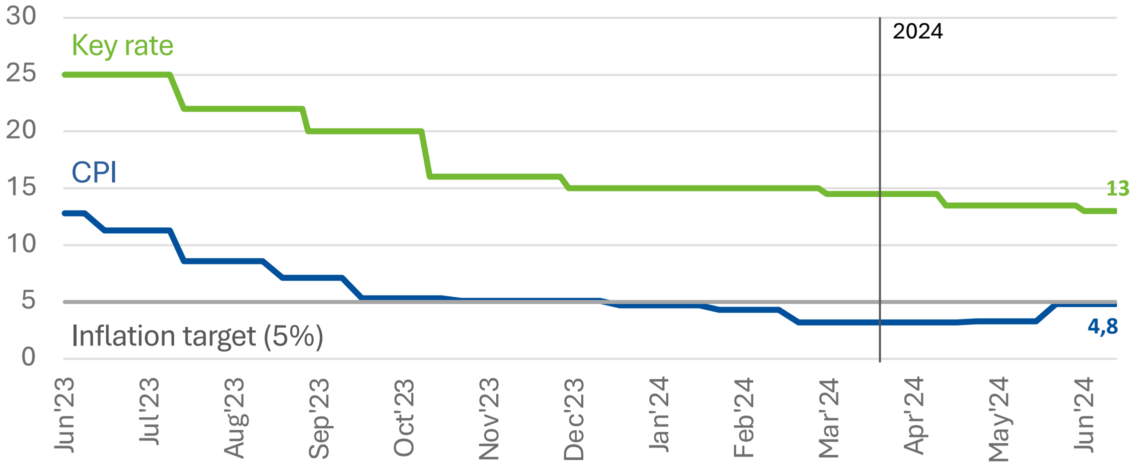
Inflation accelerates to 4.8%, and key rate policy is stable

Key rates as of June 30, 2024 (CPI y-o-y in June 2024)

Indicator	Value, %	Change in May
Government bonds rate (12-m)	14.71	-0.25 p.p.
Key rate	13.00	0.00 p.p.
12-m deposit rate	12.82	-0.49 p.p.
3-m deposit rate	13.19	-0.35 p.p.
Inflation (CPI)	4.80	1.5 p.p.

Sources: NBU, State Statistics Service, UIRD

Inflation (CPI) y-o-y and NBU key rate, %



Source: NBU, State Statistics Service

- In mid-June 2024, the NBU set the key policy rate at 13%, citing **favourable inflation trends, improved expectations**, and progress in **securing international financing** as reasons for easing monetary conditions to support lending and economic recovery.
- Opinions differ on whether to **keep the key policy rate unchanged** (13%) due to inflation risks and budget needs or to **reduce it to 12%-12.5%** by year-end.
- The yield of **one-year hryvnia war bonds** and the **3- and 12-month deposit rates** continued to decrease in response to the **reductions in the key policy rate over the last several months**.
- In June 2024, **inflation accelerated to 4.8% year-over-year** due to gradual waning of effects from last year`s harvests, pass-through effects from hryvnia depreciation, and increase in electricity prices.

MONETARY AND FX SECTOR

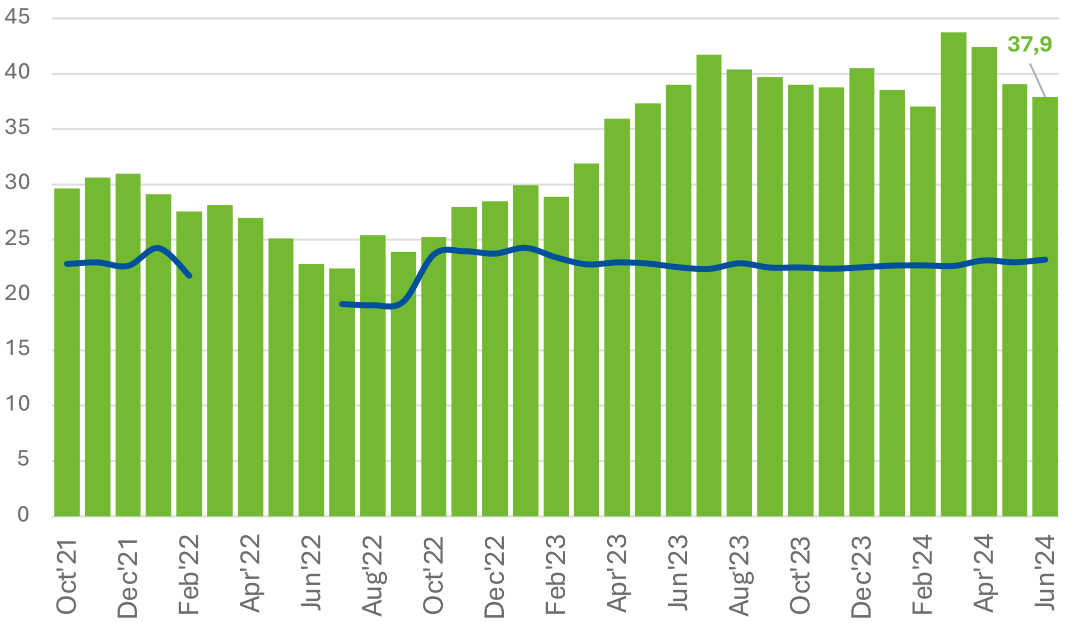
CENTRE FOR ECONOMIC STRATEGY

International reserves declined once again but remain at sufficient level

In June, **international reserves fell by 2.9% to $37.9 bn** (**4.9 months of import coverage**) due to the NBU's FX interventions to **address foreign currency deficits**, **stabilise the exchange rate**, and **make FX debt payments**, partly offset by international financial aid.

In June, the **hryvnia fluctuated but faced moderate depreciation pressure**. The spread between cash and official rates remained within 1.3%. **Increased FX demand** was driven by **high budget expenditures, intensified fuel purchases, and May`s FX liberalisation**.

Gross international reserves and their amount needed to cover 3 months of future imports, $ bn



Source: NBU. In March-June 2022, the NBU did not calculate the coverage of future imports due to the unstable situation

Average daily official and market exchange rates UAH/USD

Source: NBU (official rate), index.minfin.com.ua (cash market rate)

CENTRE FOR ECONOMIC STRATEGY

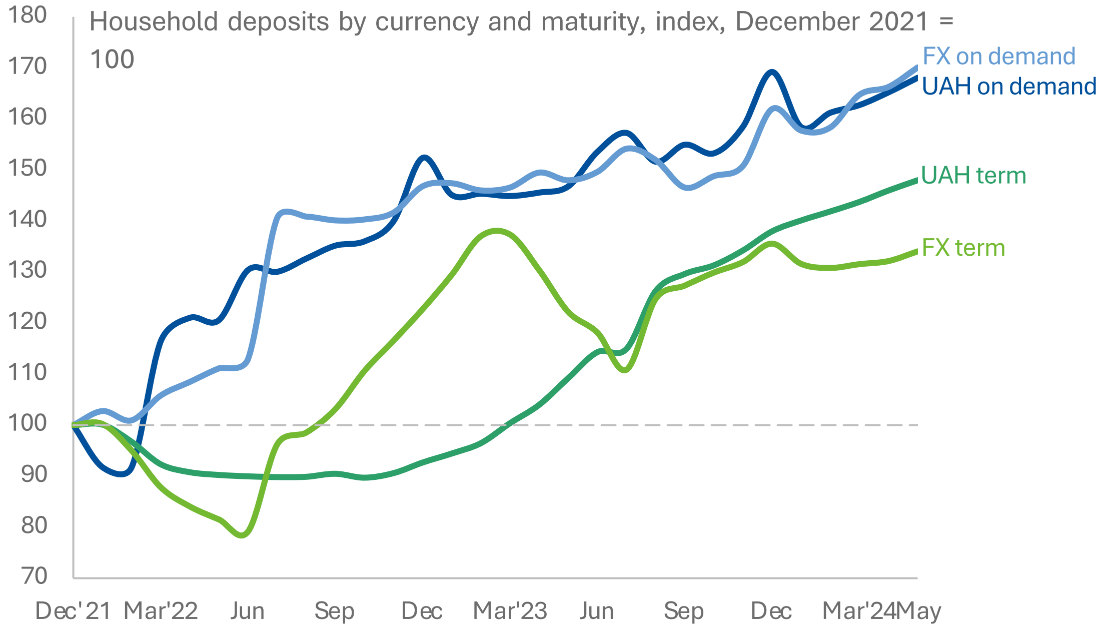
In May, household deposits continued to rise alongside corporate and retail lending

In May, **hryvnia and foreign currency deposits continued their growth**, reaching or surpassing levels seen at the end of 2023.

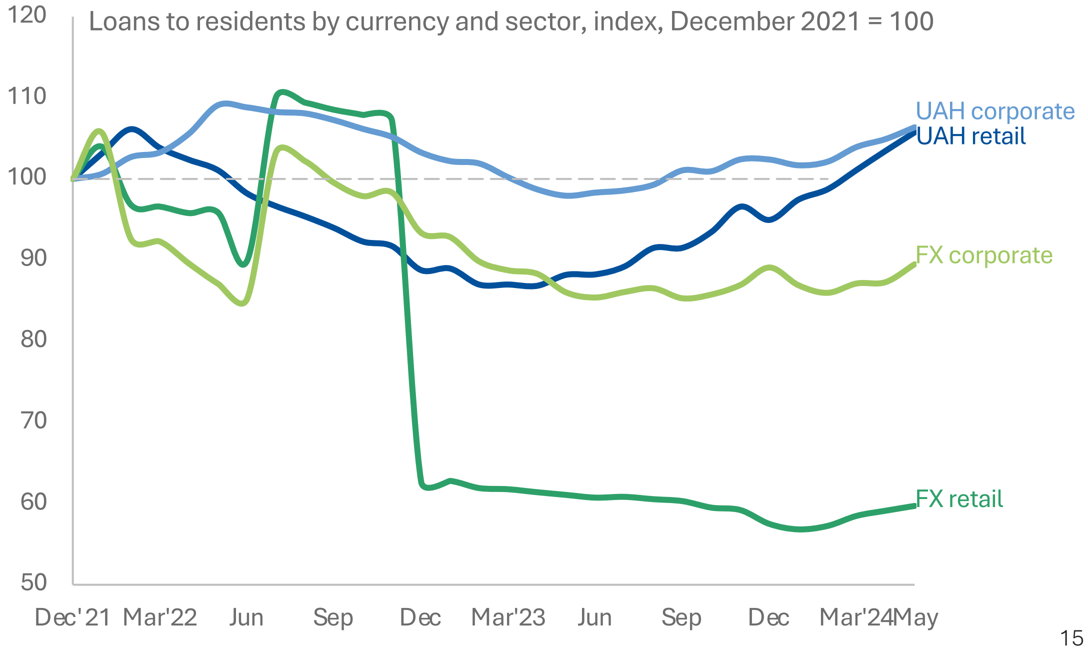
Rising incomes drive increased bank deposits, with over a third in hryvnia terms ensuring stable balances amid growing deposit competition. **Eased currency exchange rules bolster savings in foreign cash.**

Corporate and retail lending continues to recover slightly among all currencies.

Profitable sectors self-fund, bolstered post-invasion; **long-term loan demand is low**; rebuilding firms can access subsidised loans. **Some use bank loans, while others rely on external or intra-group funds.**



Source: NBU



Source: NBU

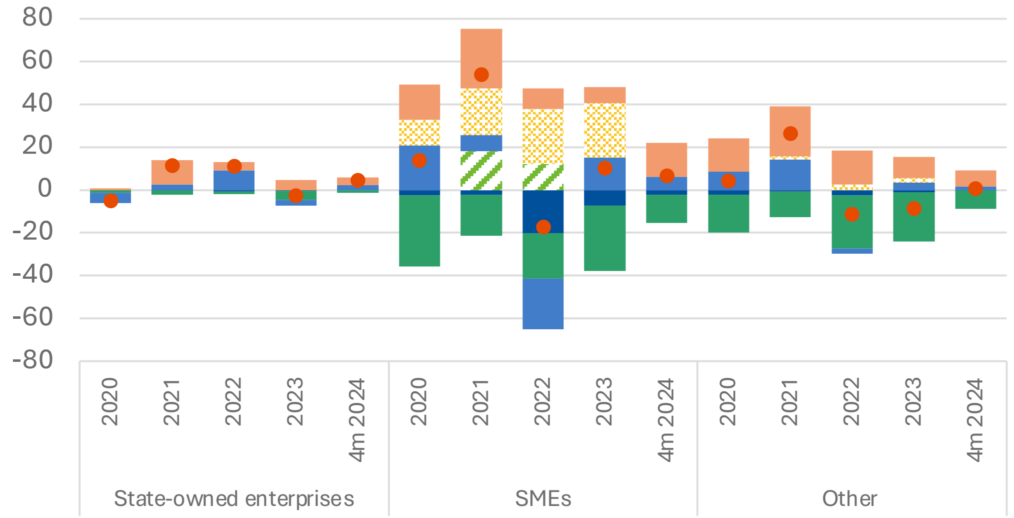
CENTRE FOR ECONOMIC STRATEGY

Stable conditions boost lending; state banks are leading in client acquisition

Acceptable macro conditions and controlled security risks are **boosting lending**, with banks lowering rates amid reduced inflation and credit risks.

Challenges like energy infrastructure damage, power disruptions, war uncertainty, and a shortage of skilled workers **continue to hinder business investment**.

Change in corporate performing loans in hryvnia, UAH bn

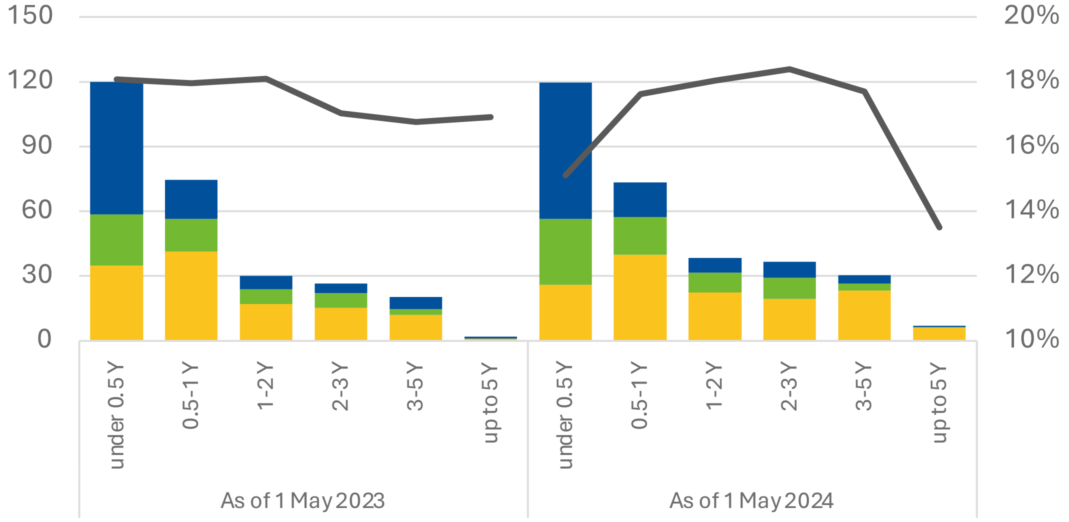


Source: NBU, BDF

Banks across all groups are increasing hryvnia loans at moderate rates, signalling systemic improvements in lending conditions and fuelling competition.

A significant factor driving increased lending is the emergence of new borrowers. State-owned banks were the most active in attracting new clients.`

Banks’ performing corporate loans in hryvnia by terms and their costs

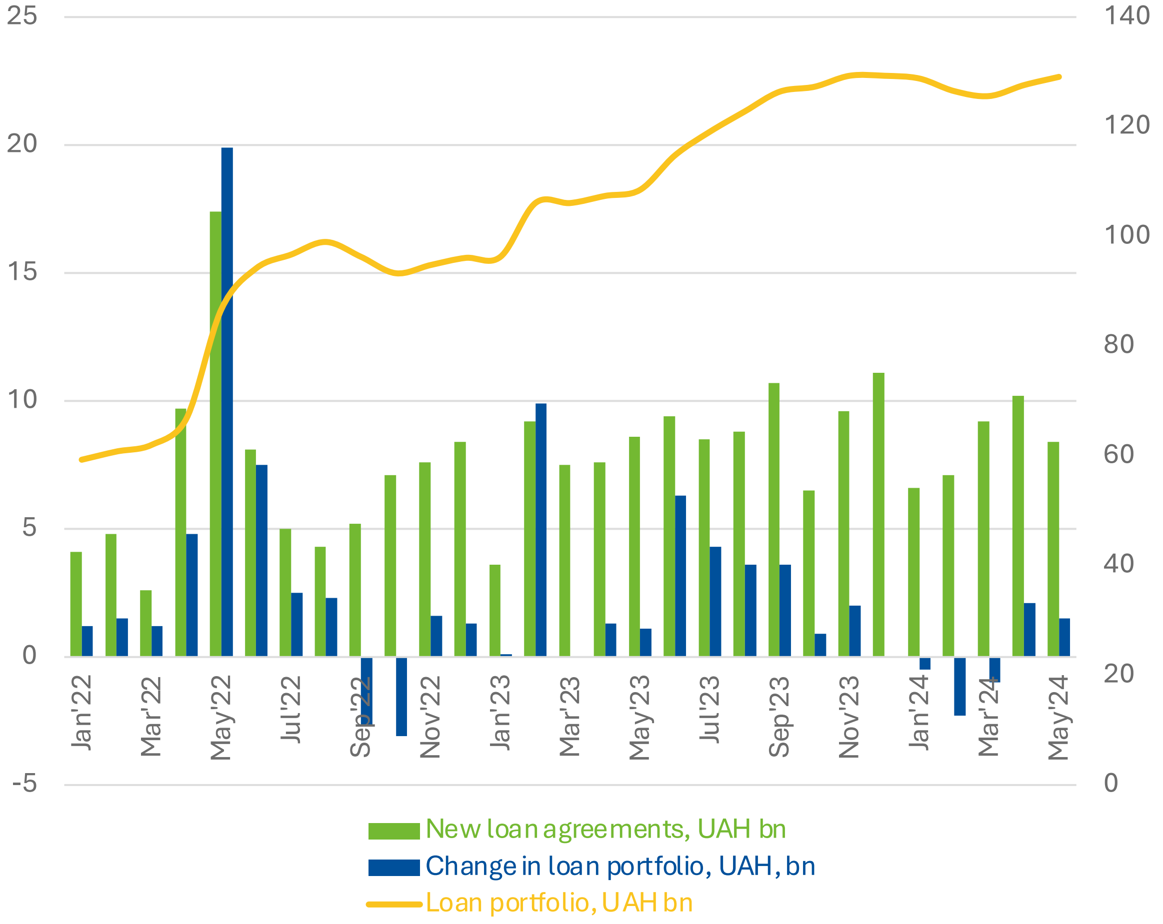


Source: NBU

CENTRE FOR ECONOMIC STRATEGY

Affordable Loans 5-7-9% were crucial during the invasion`s onset but need further refinement

Loans under the "Affordable Loans 5-7-9% program," UAH bn



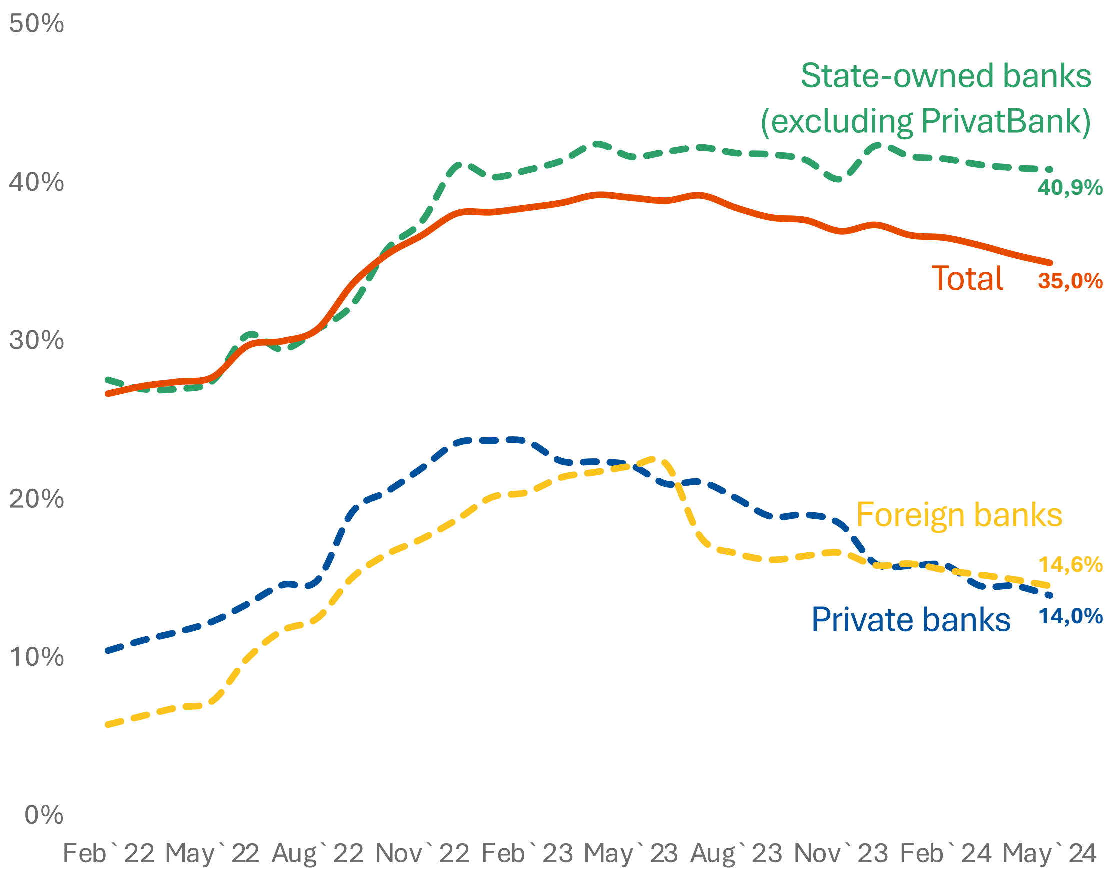
Source: BDF

- **The "Affordable Loans 5-7-9%" program was crucial during the war's first year**, enabling bank financing despite the 2022 deep economic crisis.
- Since the invasion, **the subsidised loan portfolio more than doubled to UAH 129 bn by June 2024**. Low loan costs increased state expenses. **Compensation debt to banks, over UAH 7 bn in early 2024, fell to UAH 5.8 bn by June 2024.**
- Budget constraints and imbalances prompt a redesign. In April, **limits for subsidised working capital loans were cut from UAH 60 m to UAH 5 m**, and bank margins above the UIRD index were reduced by 3–5 p. p.
- Further steps **include focusing on investment projects, providing working capital loans to select clients, regularly assessing clients' eligibility**, and considering **a loan portfolio cap based on the program's budget**.

CENTRE FOR ECONOMIC STRATEGY

In May, the NPL share decreased, but the total NPL portfolio increased

Non-performing loans by bank ownership, % of total assets



- As of May, **the share of non-performing loans (NPLs)** as a percentage of the total loan portfolio **decreased to 35%** (down from 35.5% in April).
- This reduction reflects the **increase in total lending volumes** (+ UAH 19.5 bn in May) and the corresponding **growth in the share of the healthy loan portfolio**.
- At the same time, **the non-performing loan portfolio itself increased** by UAH 1 bn in May, **reaching UAH 421.3 bn.** Notably, there was **an increase in non-performing loans to individuals,** marking the first rise **since the beginning of 2023**.
- **Most corporate NPLs**, excluding loans to former PrivatBank owners, **result in minimal payments, mainly interest**, with over two-thirds of the principal debt remaining unpaid.

Source: NBU

BANKING SECTOR

CENTRE FOR ECONOMIC STRATEGY

Lending Development Strategy (1/2)

The goal of this strategy is to **fund the rebuilding of energy infrastructure** and **boost positive lending market trends** by stimulating demand to enhance the country's defence capabilities.

This strategy prioritizes lending under martial law to defence industry companies, critical energy infrastructure, manufacturing industry, agriculture sector, and support for the recovery of businesses operating in resilience areas.

Національний банк України

- Safeguarding macrofinancial stability;
- Balancing regulatory requirements to ensure financial stability while promoting lending in line with European standards:
  - Maintaining capital requirements for banks considering the sector's condition and lending potential;
  - Adapting credit risk measurement for project financing under martial law to support priority industries.

Міністерство **фінансів** України

- Promoting an increase in the risk appetite of state-owned banks to lend to viable and economically sound projects in priority areas;
- Using state guarantees for loans in resilience areas to cover war-related losses only direct losses from war risks

МІНІСТЕРСТВО ЕКОНОМІКИ УКРАЇНИ

Further optimize and enhance government programs to target priority economic sectors and companies in resilience areas

CENTRE FOR ECONOMIC STRATEGY

Lending Development Strategy (2/2)

Strategic Goals

1. Crediting for victory
2. Ensuring the availability of credit
3. Lowering credit risk
4. Enhancing the quantity of the loan portfolio
5. Environmental responsibility
6. Developing infrastructure for SMEs
7. Financial responsibility
8. Innovations in financial services

Focuses of the Lending Strategy

Lending development under martial law

- Balancing financial stability and European lending standards
- International guarantees and investment
- Defence industry and Energy sector
- Resilience areas
- State programs and guarantees, guarantees of the BDF
- Encouraging state-owned banks to lend to priority areas

Developing a legislative framework to stimulate lending

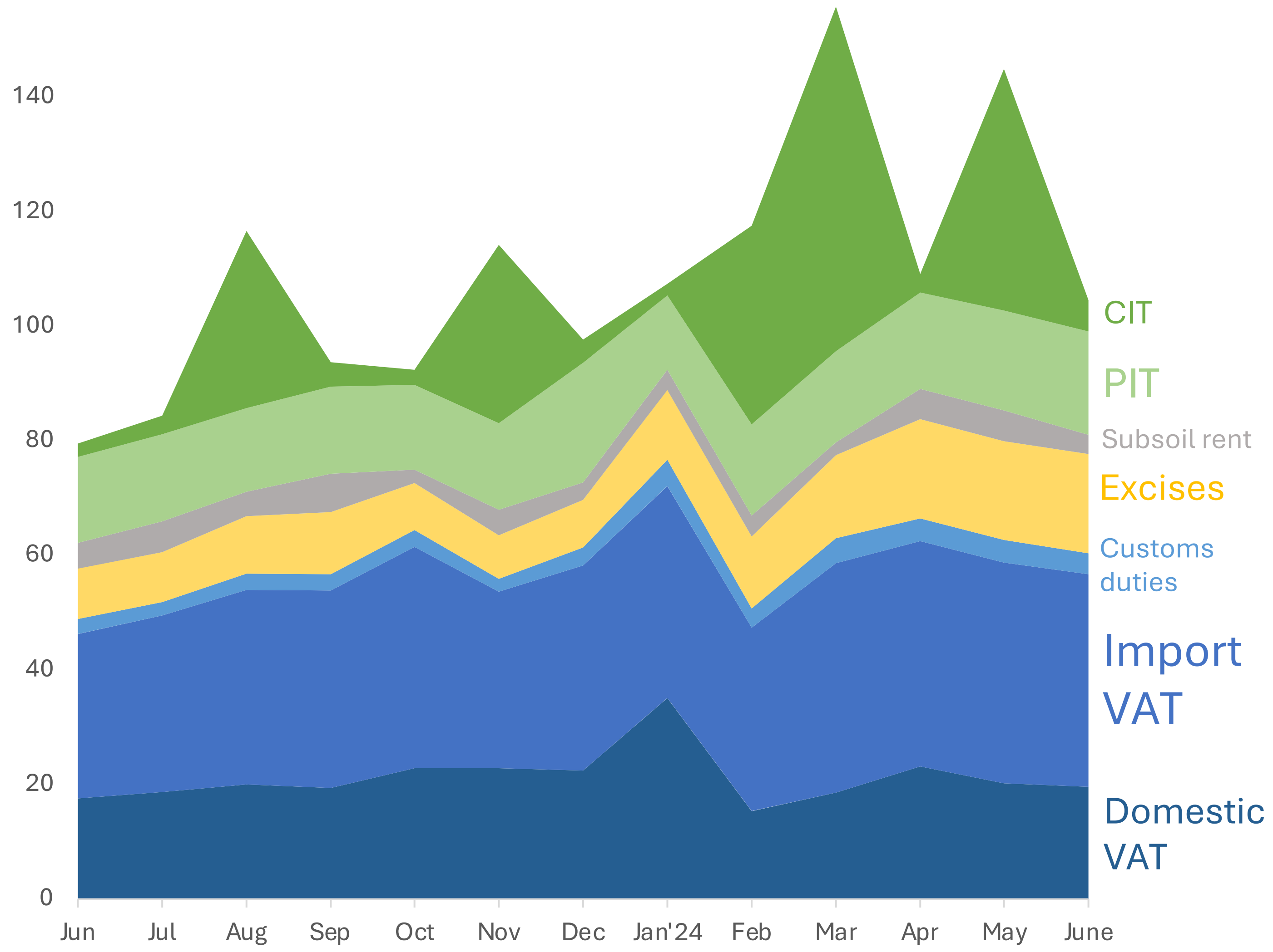
- Development of sustainable finance
- Development of mortgage lending
- Development of factoring
- Development of financial leasing
- Securitisation of financial assets

FISCAL SECTOR

FISCAL SECTOR – TAX REVENUES

1H strong growth y-o-y, but stagnating since April

State budget tax revenues, UAH bn



Sources: Ministry of Finance, National Bank

Tax revenues of the state budget in June UAH were 104.6 bn, adding up to UAH 739.4 bn in 1H 2024 (+50% vs 1H 2023).

The largest growth driver in absolute terms is the CIT (+ UAH 79.7 bn, or 117% growth vs 1H 2023).

Domestic VAT revenues in first half of 2024 grew by 49%, and **VAT on imports** – by 39%. It is worth noting that while gross domestic VAT revenues increased by 26%, the VAT refunds declined by 2.5%, indicating stricter VAT administration.

Excise revenues grew by 81% bringing additional UAH 40.8 bn in 1H2024.

Subsoil rent was the only source of revenue, which decreased in 2024 – by 21% vs 1H 2023.

Major factors behind revenue growth were increased CIT for banks, cancellation of temporary tax benefits in 2023, increased excise tax rates, transfer of “military” PIT to state budget, better administration, inflation and devaluation.

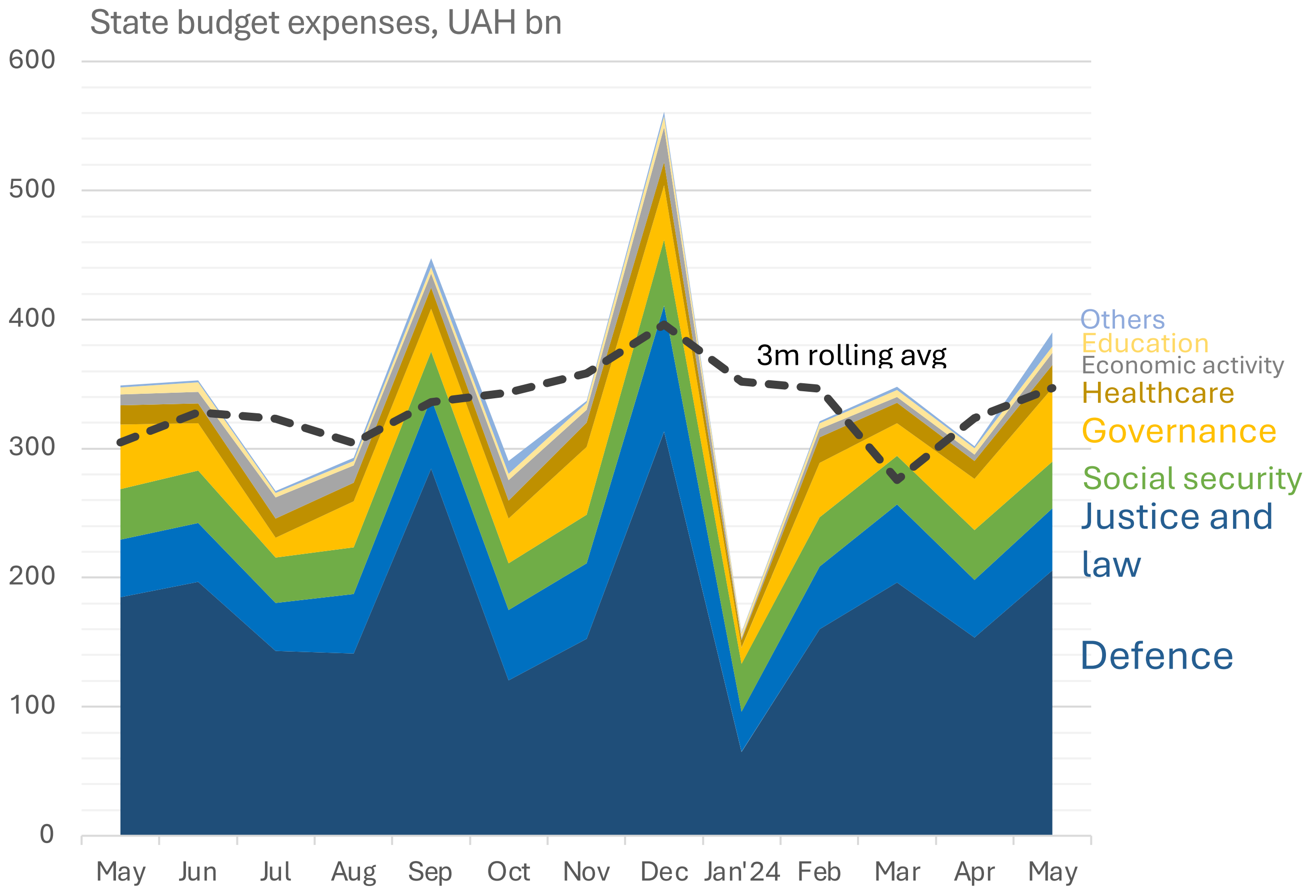
Since January, the budget also received UAH 64.2 bn of the dividends and net profits of the SOE.

FISCAL SECTOR – EXPENSES AND LOCAL BUDGETS

Moderate state expenses, growing surplus of local budgets

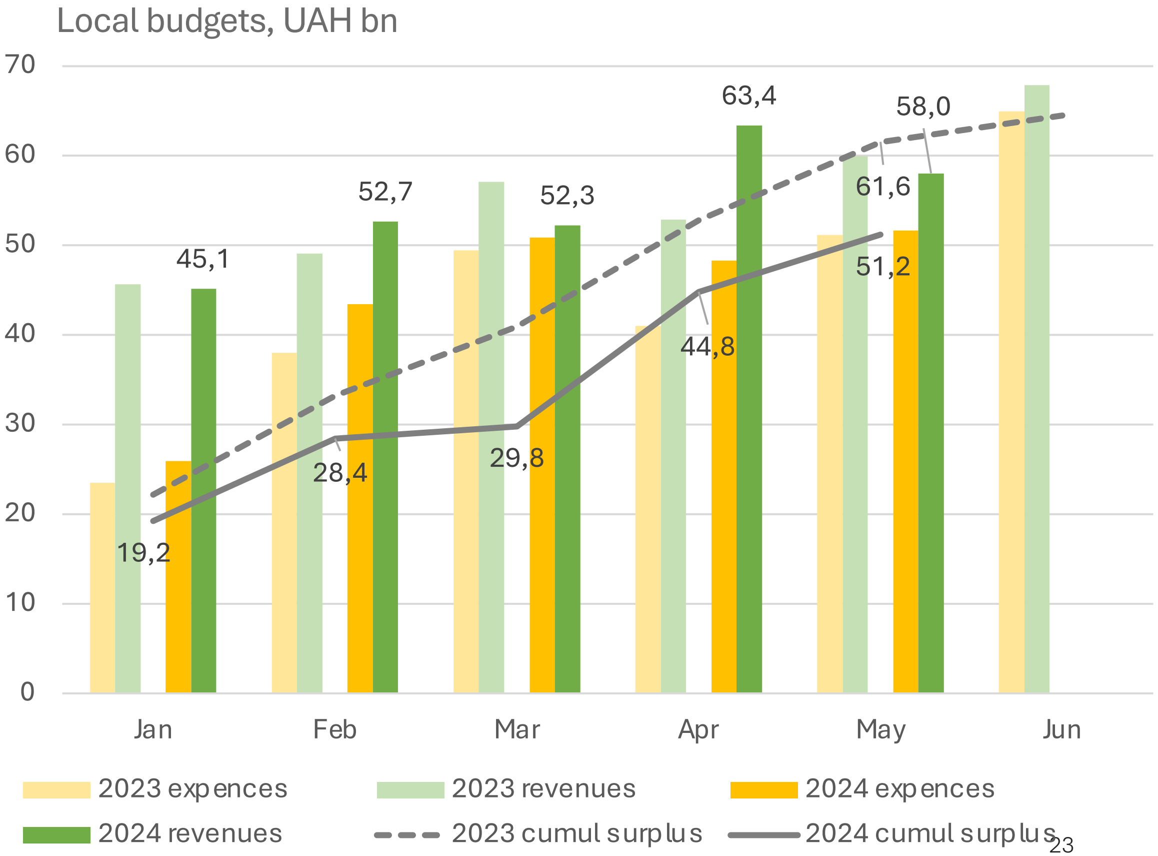
State budget expenses in May increased by 29% to UAH 390 bn, with defence spending growth of 34% m-o-m, to UAH 206 bn.

In 5m 2024 the defence made 51% of all spending.



Local budgets' cumulative surplus reached UAH 51.2 bn. This brings the estimate of unused costs, accumulated by local budgets to over UAH 160 bn.

Total revenues reached UAH 264 bn, of which 28% were transfers from the state budget.



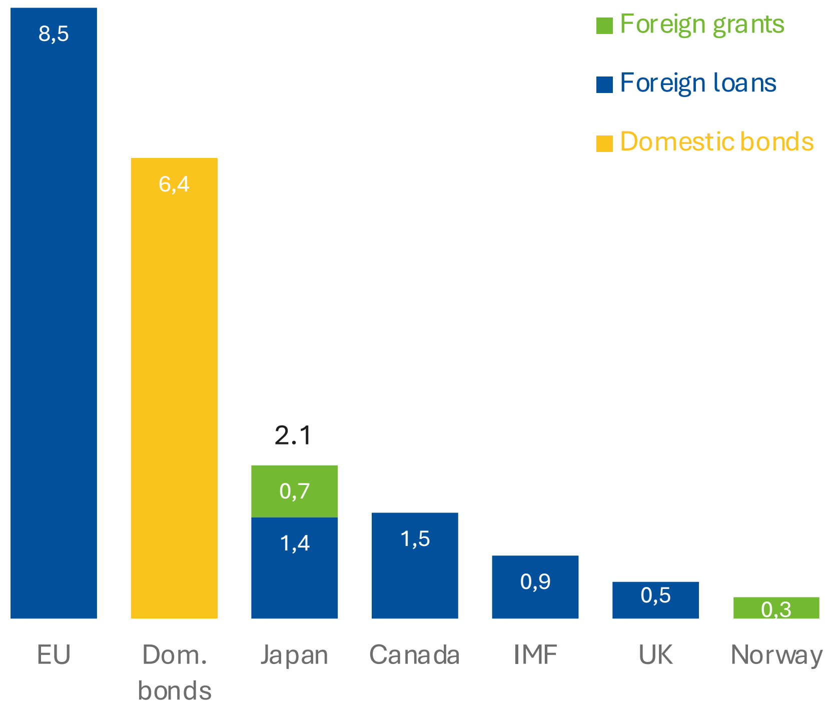
Source: Ministry of Finance *Note: only May figures were released as of the presentation date*

FISCAL SECTOR

Ukraine received $2 bn of foreign budget assistance in June

In June, foreign financial assistance increased after a drop in May: Ukraine received $2 bn from the European Union and $3 million from the World Bank (both as loans).

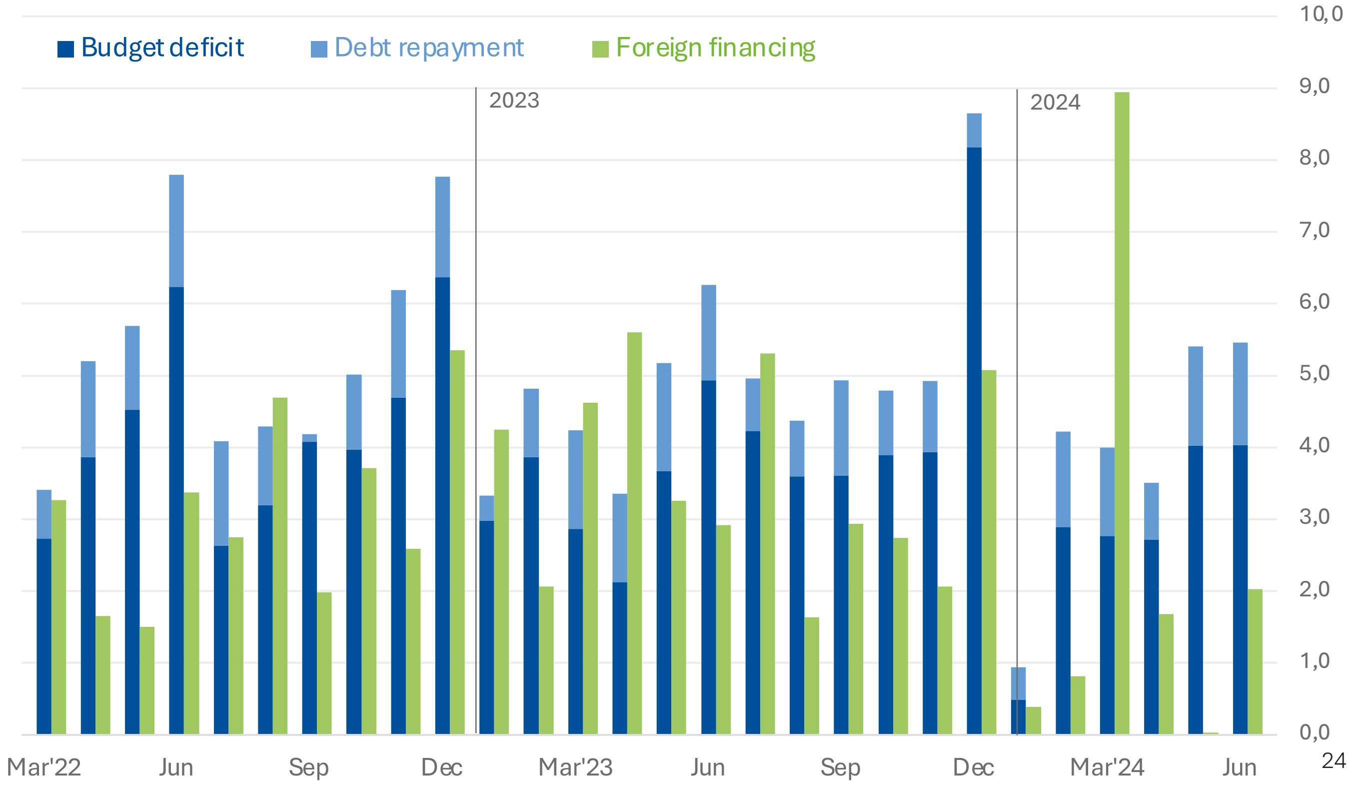
2024 additional financing of Ukraine's state budget as of June 28, $ bn



World Bank — $23 m, Spain — $3 m. Source: Ministry of Finance

In June, foreign aid covered about 37% of the state budget financing needs. Although this is an improvement compared to May (0.4% coverage), the situation is still far from ideal. In addition, disbursements of American budgetary aid have not yet begun.

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



Source: Ministry of Finance, NBU, CES calculations

CENTRE FOR ECONOMIC STRATEGY

SPECIAL TOPIC: BUSINESS ACCESS TO FINANCE

Government of the Netherlands

The project "Survey of Access to Finance for Ukrainian SMEs" is implemented with the support of the Ministry of Foreign Affairs of the Netherlands within the framework of the Netherlands' foreign development policy, funded by the Private Sector Development Program of the Netherlands Enterprise Agency (RVO.nl)

RECOVERY NEEDS ASSESSMENT

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Direct damage	Economic, social and other monetary losses	Recovery and reconstruction needs
$152 bn	**$499 bn**	**$486 bn**

Source: The Third Ukraine Rapid Damage and Needs Assessment (RDNA3)

AVAILABLE SOURCES OF FUNDING

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- **Bank financing:** Affordable loans 5-7-9, other lending in national currency, lending in foreign currency.
- **Non-bank loans:** Leasing companies, credit unions, financial companies
- **State and regional support programs:** eRobota, Export Credit Agency, regional, city and local programs.
- **International donors:** USA (USAID, WNISEF), European Investment Bank, European Bank for Reconstruction and Development, International Finance Corporation, Germany (GIZ, KfW), the United Kingdom, other countries and international organizations.
- **Private companies and organizations**

MAIN REQUIREMENTS FOR FUNDING RECIPIENTS

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- **Transparency and integrity of the business and its key beneficiaries**
- **A realistic business plan**
- **Operating in certain industries**
- **Operating in certain regions**
- **Appropriate collateral**
- **Compliance with the special requirements of individual programs**
- **Previous experience in obtaining credit or grant funding**
- **No ties with the aggressor country**

AMOUNT OF FUNDING IN 2024

CENTRE FOR ECONOMIC STRATEGY

5 7 9 доступні кредити

UAH 101 bn
5-7-9 Program

UAH 104 bn
Other bank credit in UAH

UAH 43 bn
Bank credit in foreign currency

Bank credits (cumulative):
UAH 248 bn

UAH 44 bn
International support

UAH 27 bn
Financial leasing

є робота
ECA Export Credit Agency

UAH 16 bn
State and regional programs

Other

UAH 7 bn
Financial companies, other companies and organizations

TOTAL:
341
UAH BN

Source: CES estimation, June 2024

KEY RECOMMENDATIONS TO GOVERNMENT AGENCIES

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- War risk insurance
- Removing barriers to the acceptance of different asset classes as collateral
- Implementation of the Lending Development Strategy
- Gradual liberalization of the leasing, mortgage and other financial services markets
- Easing restrictions on the repayment of existing external debt
- Clear focus of the state program Affordable Loans 5-7-9

KEY RECOMMENDATIONS TO BORROWERS

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- Adhere to the principles of business integrity and transparency
- Provide banks with detailed information about the company's activities
- Improve skills in preparing loan applications and business plans
- Diversify sources of financing
- Increase the organizational capacity of businesses to raise debt capital
- Use the opportunities of business associations to attract financing

OTHER RECOMMENDATIONS

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- Create a map of opportunities for Ukrainian business
- Provide companies with personalized support from commercial banks in the process of granting loans, and, if necessary, inform them about alternative sources of financing
- Adapt internal scoring models of banks to avoid unfair conditions in granting loans
- Promote the possibility of loans from credit unions and financial institutions

CENTRE FOR ECONOMIC STRATEGY

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THANK YOU.

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