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Economy review in August

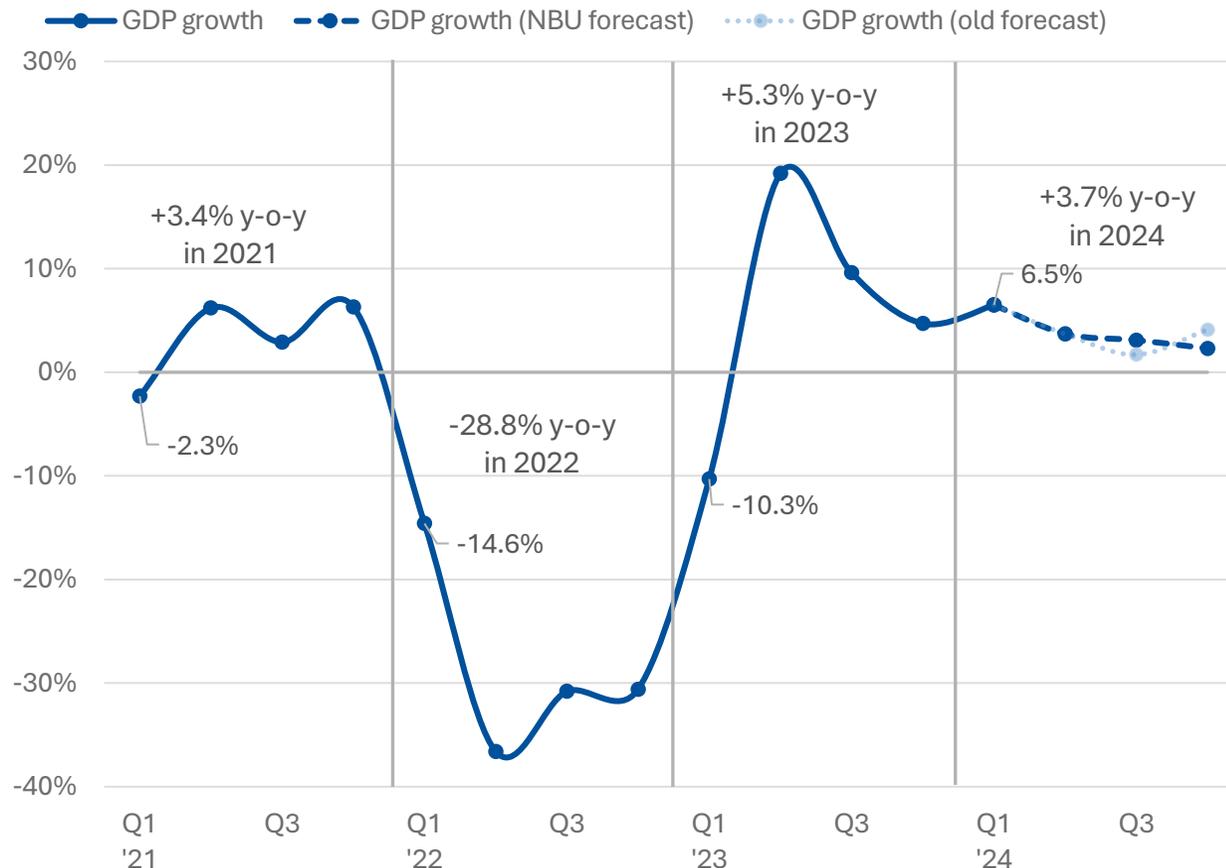
Special topic: Drought and war: how this year's harvest will impact Ukraine's economy

MACROECONOMIC TRENDS

MACROECONOMIC TRENDS

IMF forecasts GDP growth by 3% in 2024: lower than NBU forecast of 3.7%

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



Source: State Statistics Service of Ukraine, NBU

- Ukraine's economic growth will slow down in the second half of 2024, with real GDP growth of 3% for the year, according to the IMF.
- Economic growth in Ukraine will slow down due to the consequences of Russian attacks on energy infrastructure, the impact of the war on the labour market and the level of business expectations.
- According to the Ministry of Economy, in July 2024 Ukraine's GDP grew by 2.7% y-o-y. As a result, for the first seven months of this year, GDP growth is estimated at 4.0% y-o-y.

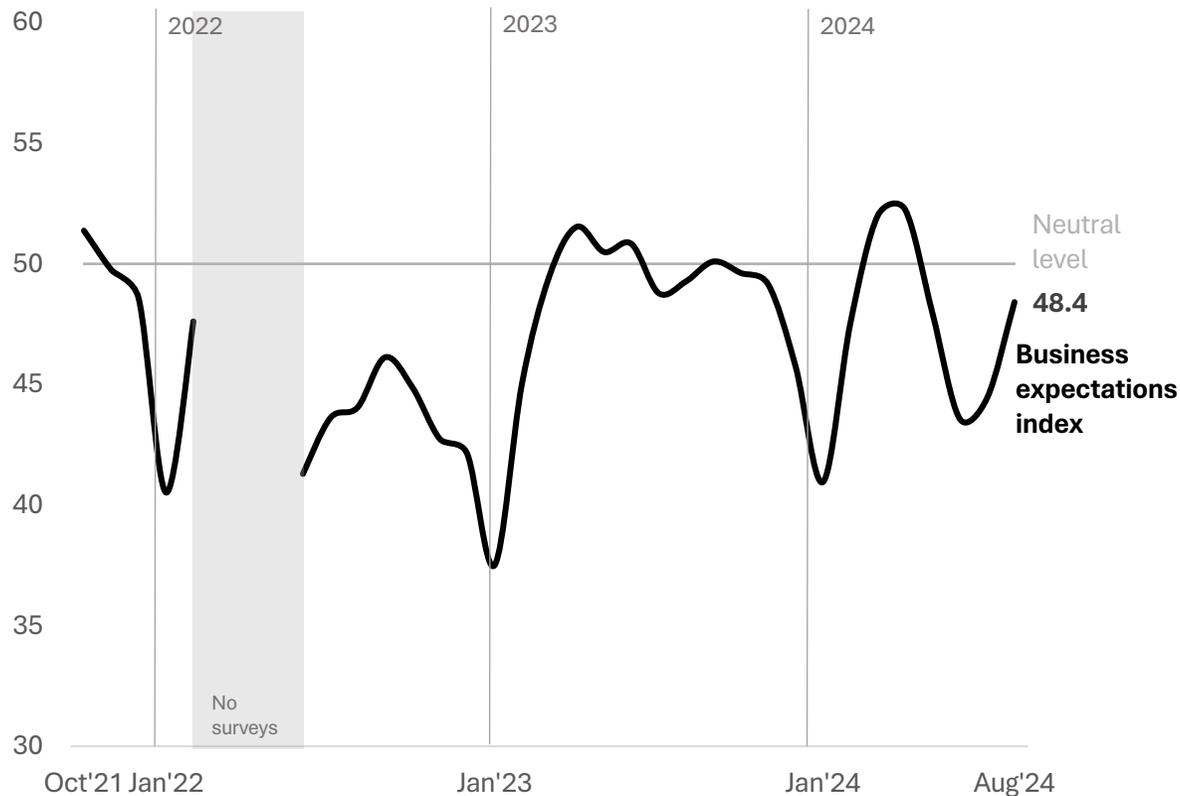
MACROECONOMIC TRENDS

Business expectations improved in August

- In August, the NBU’s business activity expectations index improved to 48.4, up from 44.4 in July, but still below the neutral level of 50 points.

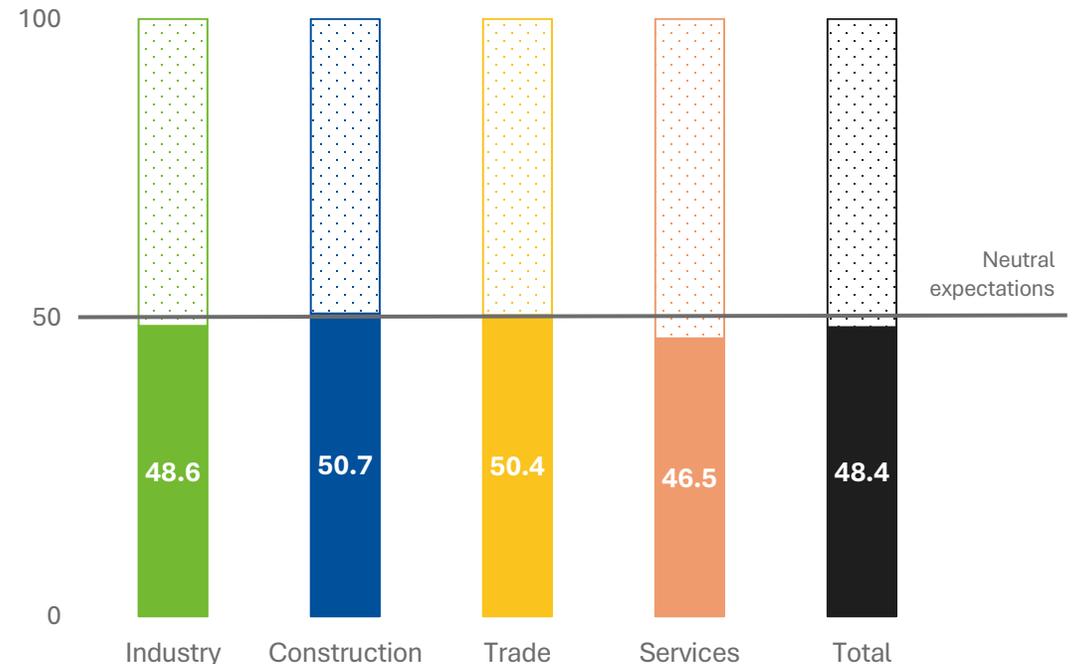
- Sentiment in all sectors surveyed improved, with construction and trade even turning positive. Sustained domestic demand, further adaptation to the power outages, and stable logistics improved business sentiment.

NBU business activity expectations index dynamics



Source: NBU

NBU business activity expectations index by sector in August





MONETARY, FX AND BANKING SECTORS

MONETARY AND FX SECTOR

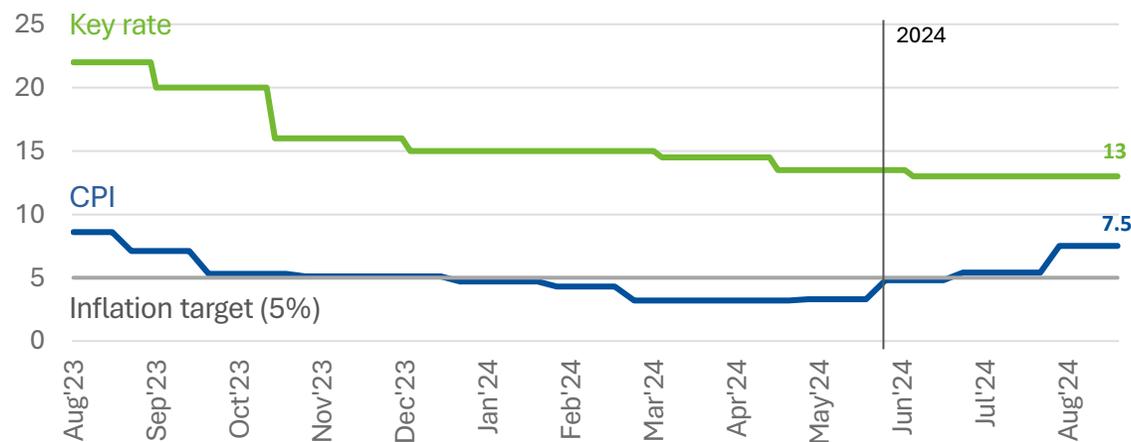
Inflation accelerates to 7.5%, and key rate policy remains the same – 13%

Key rates as of August 31, 2024 (CPI y-o-y in August 2024)

Indicator	Value, %	Change in August
Government bonds rate (12-m)	14.65	0.00 p.p.
Key rate	13.00	0.00 p.p.
12-m deposit rate	12.81	-0.20 p.p.
3-m deposit rate	12.98	-0.10 p.p.
Inflation (CPI)	7.50	2.10 p.p.

Sources: NBU, State Statistics Service, UIRD

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



Source: NBU, State Statistics Service

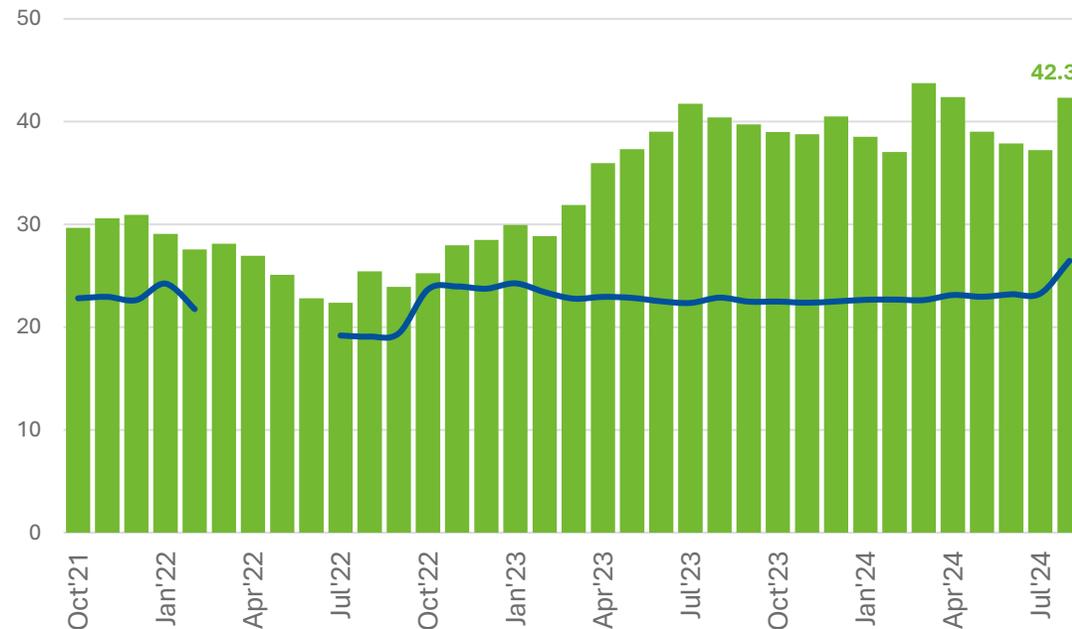
- The key policy rate has been held steady at 13% since the end of July 2024, with the goal of sustaining the FX market, safeguarding households' hryvnia savings, and aligning inflation with the 5% target over the forecast period.
- The next decision of the NBU Board on the key policy rate will be held on September 19th.
- Nominal hryvnia interest rates are falling due to the NBU's previous easing of interest rate policy. Despite this, yields still surpass both the NBU's inflation projections and households' inflation expectations, shielding hryvnia savings from inflation.
- In August 2024, inflation accelerated to 7.5% year-over-year (while in +0.6% m-o-m), driven by the poor harvest, higher business costs, and hryvnia's recent depreciation.

MONETARY AND FX SECTOR

International reserves resumed its growth, while hryvnia slightly depreciated

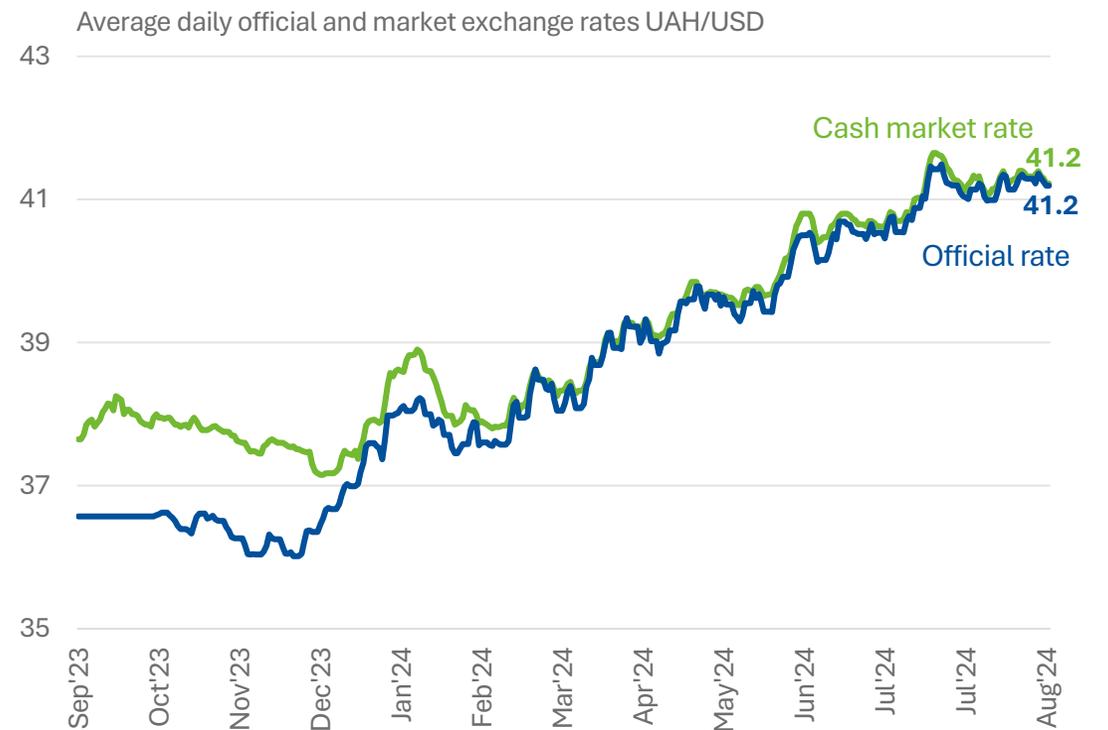
In August, international reserves grew by 13.7% to \$42.3 bn (5.4 months of import coverage) due to large inflows (\$8.5 bn) from the international partners, which exceeded the NBU's next FX sales (\$2.7 bn) and Ukraine's FX public debt servicing and payments (\$1.1 bn).

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

In August, the FX market improved with steady foreign currency supply, reduced demand, and support from international aid, leading to better exchange rate expectations. Hryvnia slightly depreciated, and the cash-to-official exchange rate spread narrowed to 0.4%.



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

BANKING SECTOR

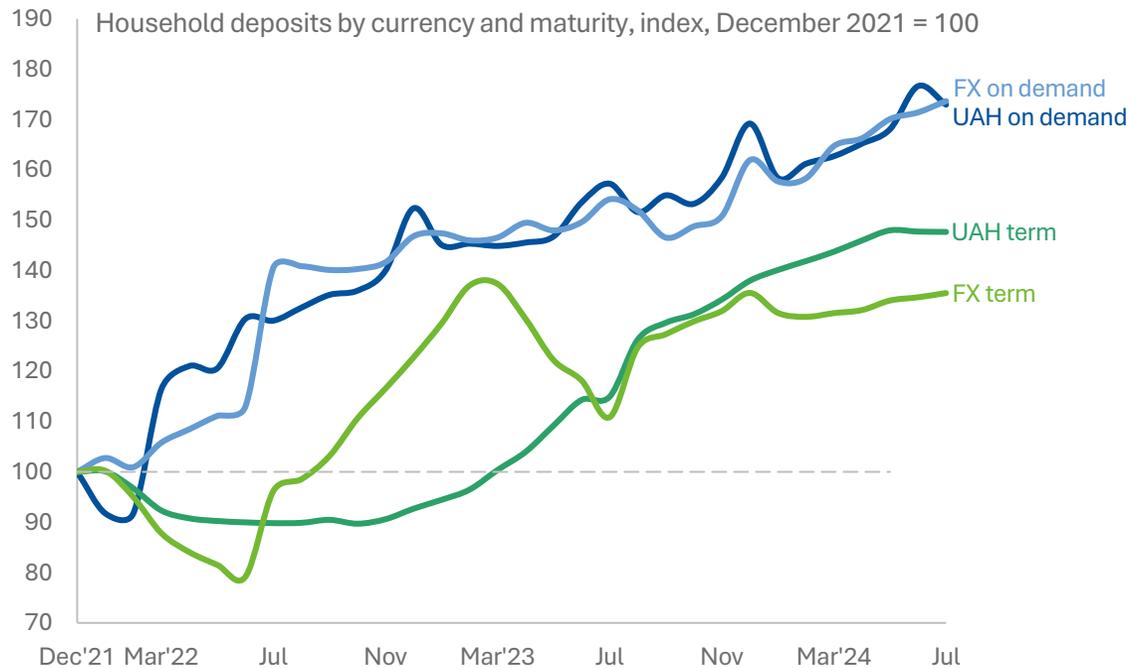
FX household deposits resumed growth, along with UAH and FX corporate and retail loans

Hryvnia term and on-demand deposits have shown a decline in volumes, while foreign currency deposits have resumed growth.

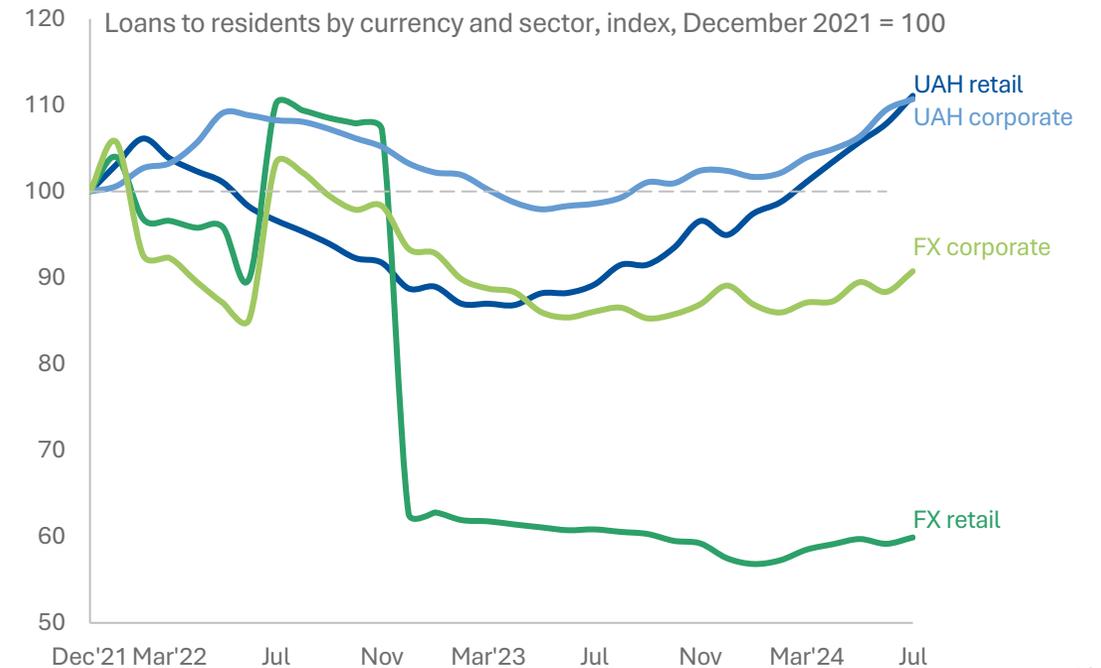
Household term deposit growth in hryvnia has stalled likely due to worsening exchange rate expectations and increased spending on energy equipment.

In July, UAH corporate and retail lending continued to recover modestly, with lending in foreign currencies resuming.

Banks approved UAH 5.8 bn in loan applications for energy infrastructure restoration projects from June 1 to September 1, 2024.



Source: NBU



Source: NBU

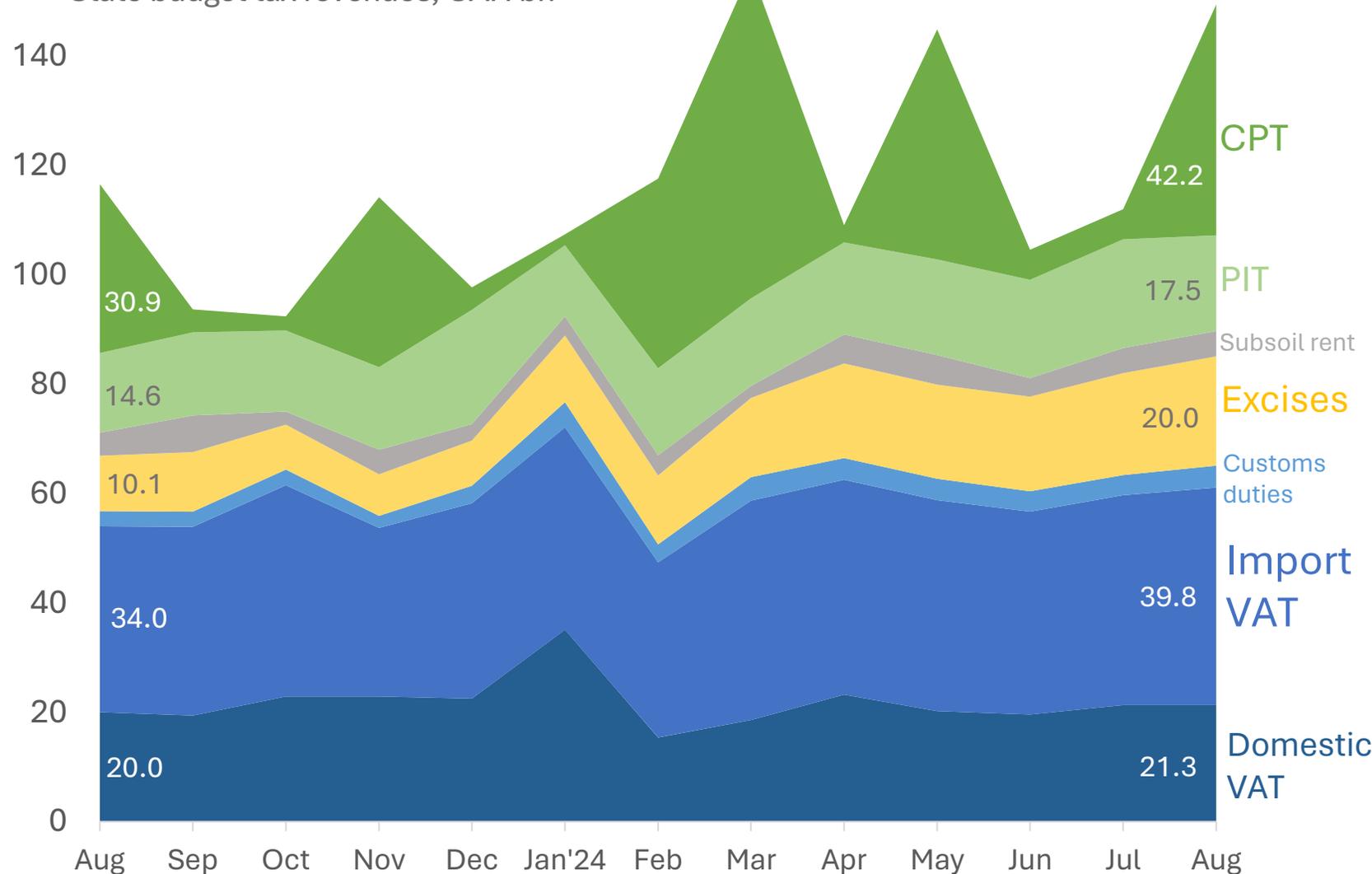


FISCAL SECTOR

FISCAL SECTOR – TAX REVENUES

Tax revenues strong and growing

State budget tax revenues, UAH bn



Tax revenues of the state budget in August were UAH 149.4 bn, adding 28% y-o-y.

The growth was driven by CPT (primarily taxation of banks with 25% tax rate), PIT (transfer of “military” PIT from the local budgets), and excises (better administration).

The Parliament is expected to consider **tax increase package** in the coming weeks to address the budget gap, however the design is yet not decided.

Likely options: increased military levy from personal income (5%), military levy for private entrepreneurs (1% for 3rd group), CPT advances for fuel retailers

The 50% windfall CPT for banks is discussed, with strong support from deputies and Tax Committee and strong opposition from MoF and NBU.

VAT increase is not on the table.

Source: Ministry of Finance. Note: based on the preliminary budget performance data, released by the MoF

FISCAL SECTOR – STATE BUDGET EXPENSES

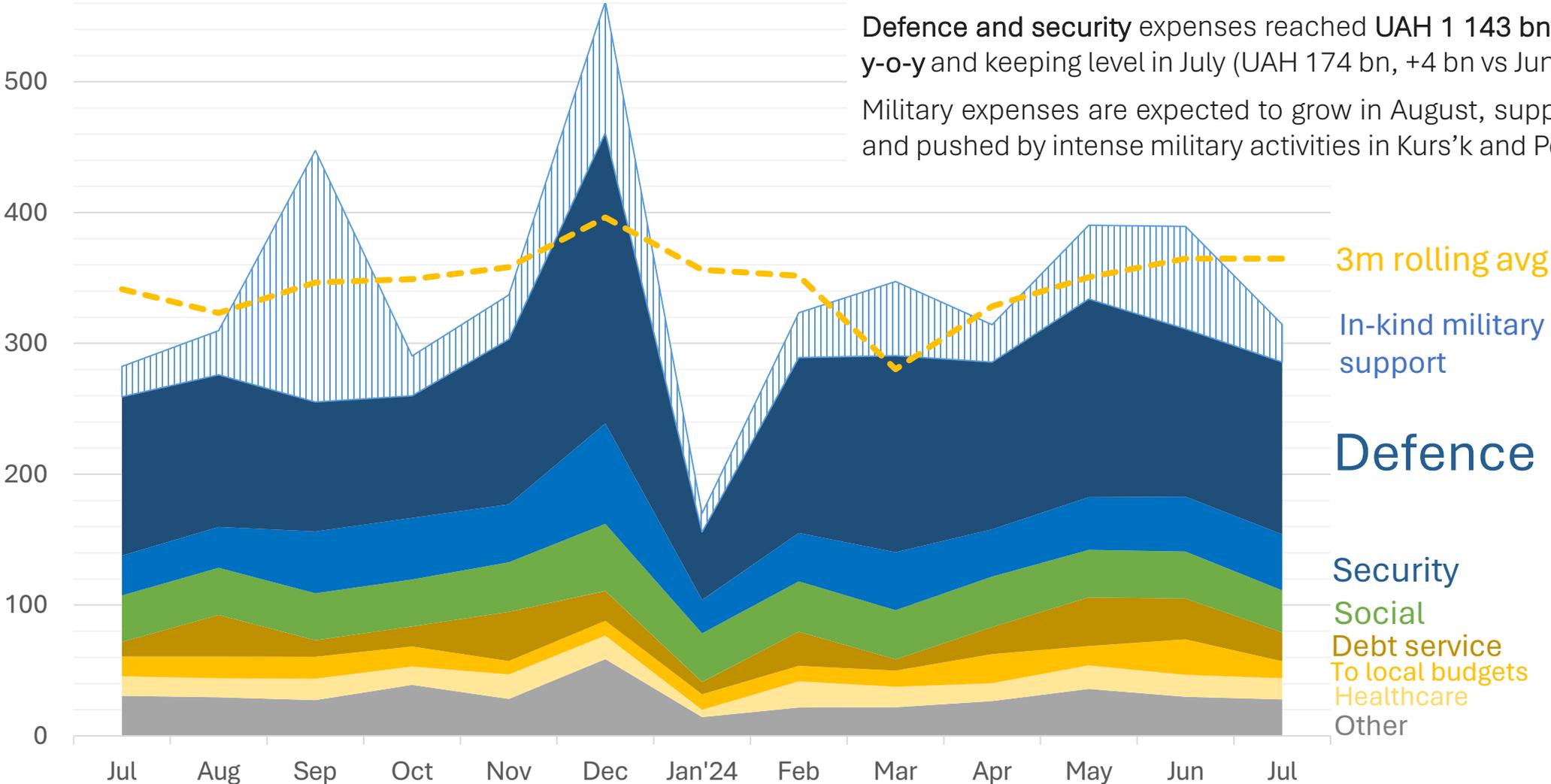
Defence spending is limited by own revenues, military support decreased

State budget expenses net of in-kind military support reached UAH 1,952 bn for 7m 2024, adding 11.6% y-o-y.

Defence and security expenses reached UAH 1 143 bn for 7m2024, adding 16% y-o-y and keeping level in July (UAH 174 bn, +4 bn vs June).

Military expenses are expected to grow in August, supported by strong revenues and pushed by intense military activities in Kurs'k and Pokrovs'k directions.

State budget expenses, UAH bn



Source: Ministry of Finance. Note: only July figures were released as of the presentation date

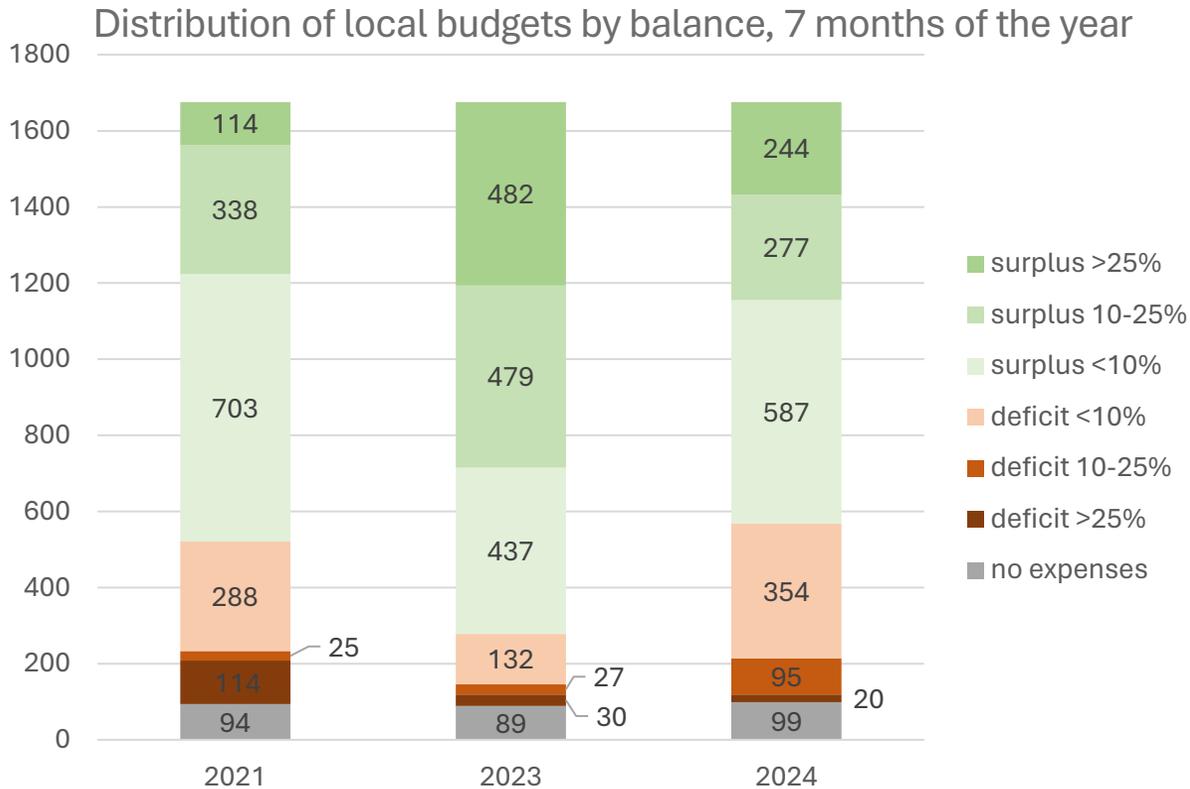
FISCAL SECTOR – LOCAL BUDGETS

The revenue structure changed, direct taxation weight growing

Total revenues for 7 months remained on par with 2023 (UAH 381.5 bn vs UAH 383.3 bn).

The distribution of budgets by balance is returning to pre-war pattern (over half of the budgets deviate within 10% of 0 balance). The re-allocation of military PIT pushed the share of deficit budgets from 11 to 28%.

Local budgets' loss of military PIT is partially compensated by local taxes (single tax and property tax), CPT, and excises, an increase in transfers from the state budget (+ UAH 6.1 bn), and UAH 3.9 bn of non-tax revenues, including asset sales.



Source: Ministry of Finance, CES calculations

Changes in tax revenue sources, UAH bn



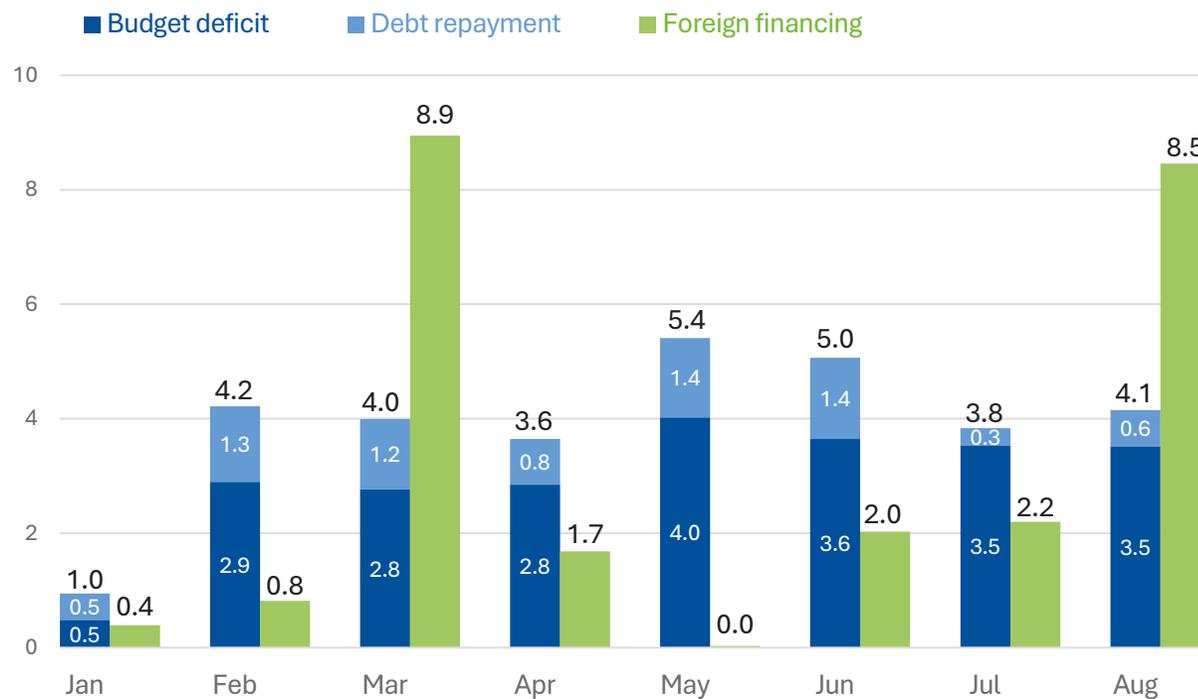
FISCAL SECTOR

Ukraine received \$8.5 bn of foreign assistance in August

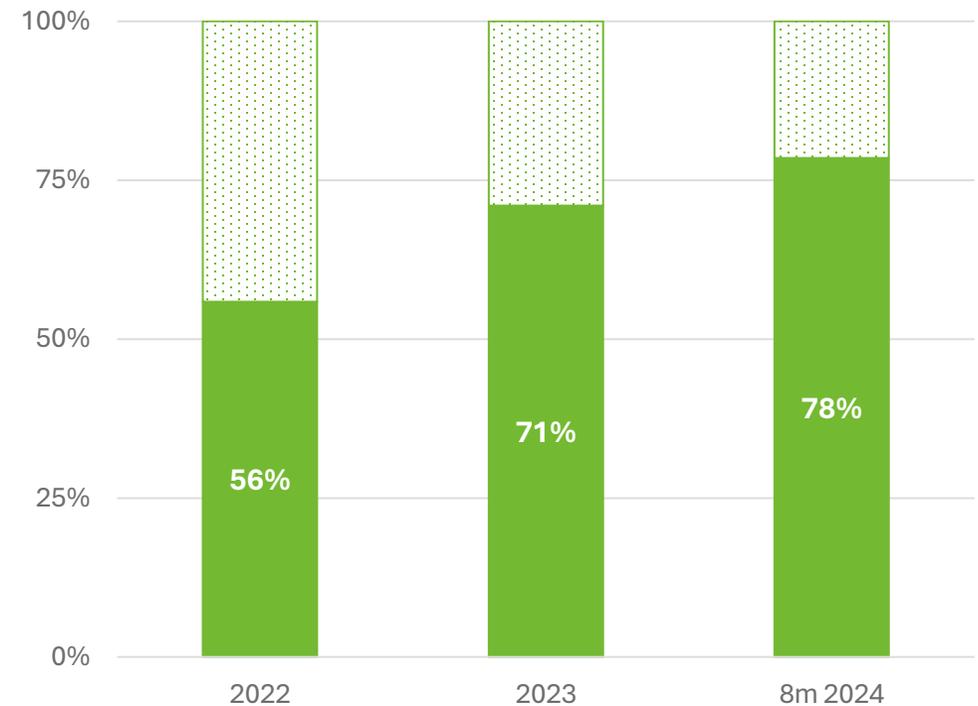
In August, Ukraine received \$8.5 billion in foreign financing for the state budget: \$4.5 billion from the EU (\$1.6 billion in grants, the rest in soft loans) and \$3.9 billion in grants from the US. The Ukrainian government says that the need for foreign financing this year will be fully covered. However, next year is still shrouded in uncertainty.

Foreign aid covered 78% of the additional needs of the state budget in 8 months of 2024, which is better than in 2022 and 2023. However, this share is expected to decline in the coming months due to a decrease in the amount of monthly disbursements.

Foreign financing, state budget deficit and debt repayment in 2024, \$bn



State budget financial needs coverage by foreign financing, %



Sources: Ministry of Finance, NBU, CES calculations



SECTORAL ANALYSIS

SECTORAL ANALYSIS

Electricity deficit decreases after hot August despite massive Russian shelling

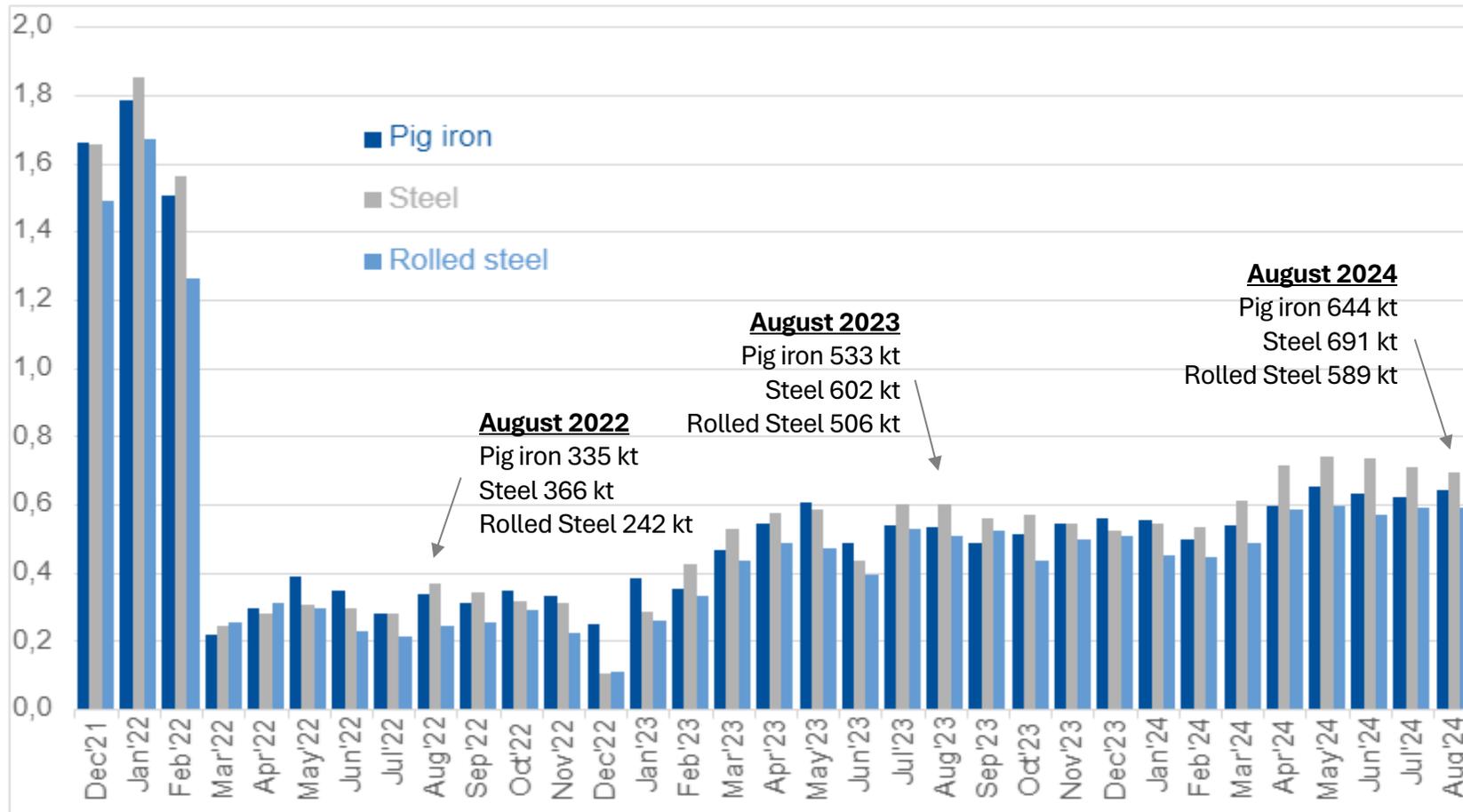
- In August, Ukraine imported 461 GWh of electricity. This is almost half as much as in each of the previous two months, but still the third highest monthly figure since the start of the full-scale invasion.
- On August 25, daily imports dropped to 4 GWh, the lowest level since early May, but the next day **Russia launched the most massive shelling of Ukrainian energy facilities in history**. More than 100 missiles were shot down, but dozens more caused further damage to energy facilities.
- The Supervisory Board of Ukrenergo has dismissed Volodymyr Kudrytskyi from the position of the Chairman of the Board. International financial organizations are concerned about Kudrytskyi's dismissal, as it could affect the stability of Ukraine's energy system and worsen its investment climate.
- Energoatom announced that the company is “preparing to implement the Chyhyryn NPP construction project” following Ukraine's energy strategy until 2050. It promised to install four AP1000 power units based on the Westinghouse technology.



SECTORAL ANALYSIS

Steel production declines again, but still higher than in 2023

Ukraine ferrous production by main categories, mt

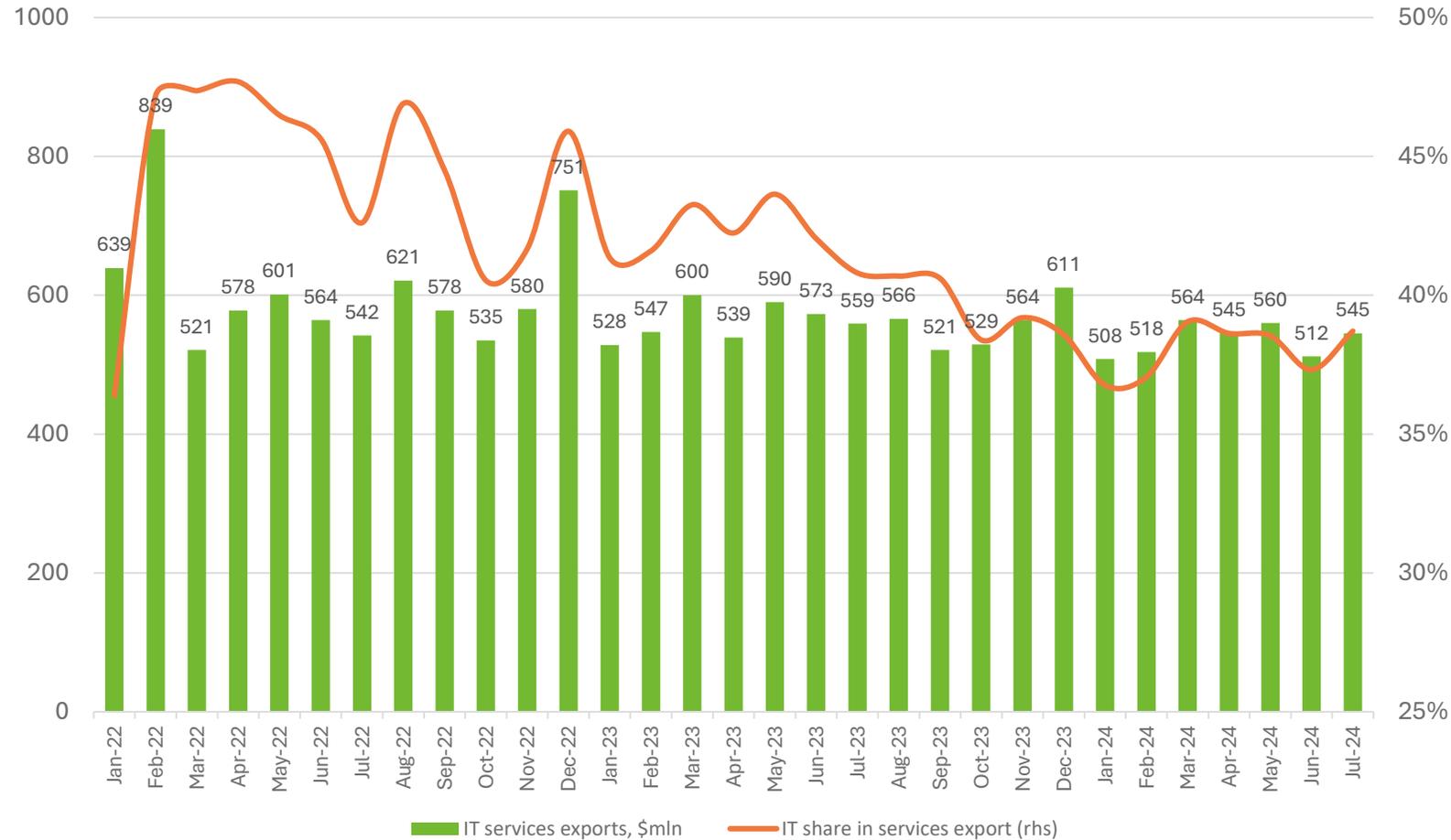


Source: Ukrmetalurgprom

- In August, **Ukraine produced** 644 kt of pig iron (+4% m-o-m), **691 kt of steel (-3%)** and 589 kt of rolled products (0%). In total for 8m2024, production of the main types of steel products increased by 21-31%.
- **Global iron ore prices fell to \$91/t**, the lowest since 2022. The price decline since the beginning of the year was 36%.
- **Global steel prices are fluctuating around \$420/t**, driven by cooling domestic demand in China and the entry of cheaper Chinese steel into the global market.
- In January-July 2024, **Ukraine increased the import of flat rolled products** by 22% y-o-y – up to 565 kt. Turkey remains the key supplier with 105 kt.

SECTORAL ANALYSIS

IT industry hires after staff cuts in the first half of the year



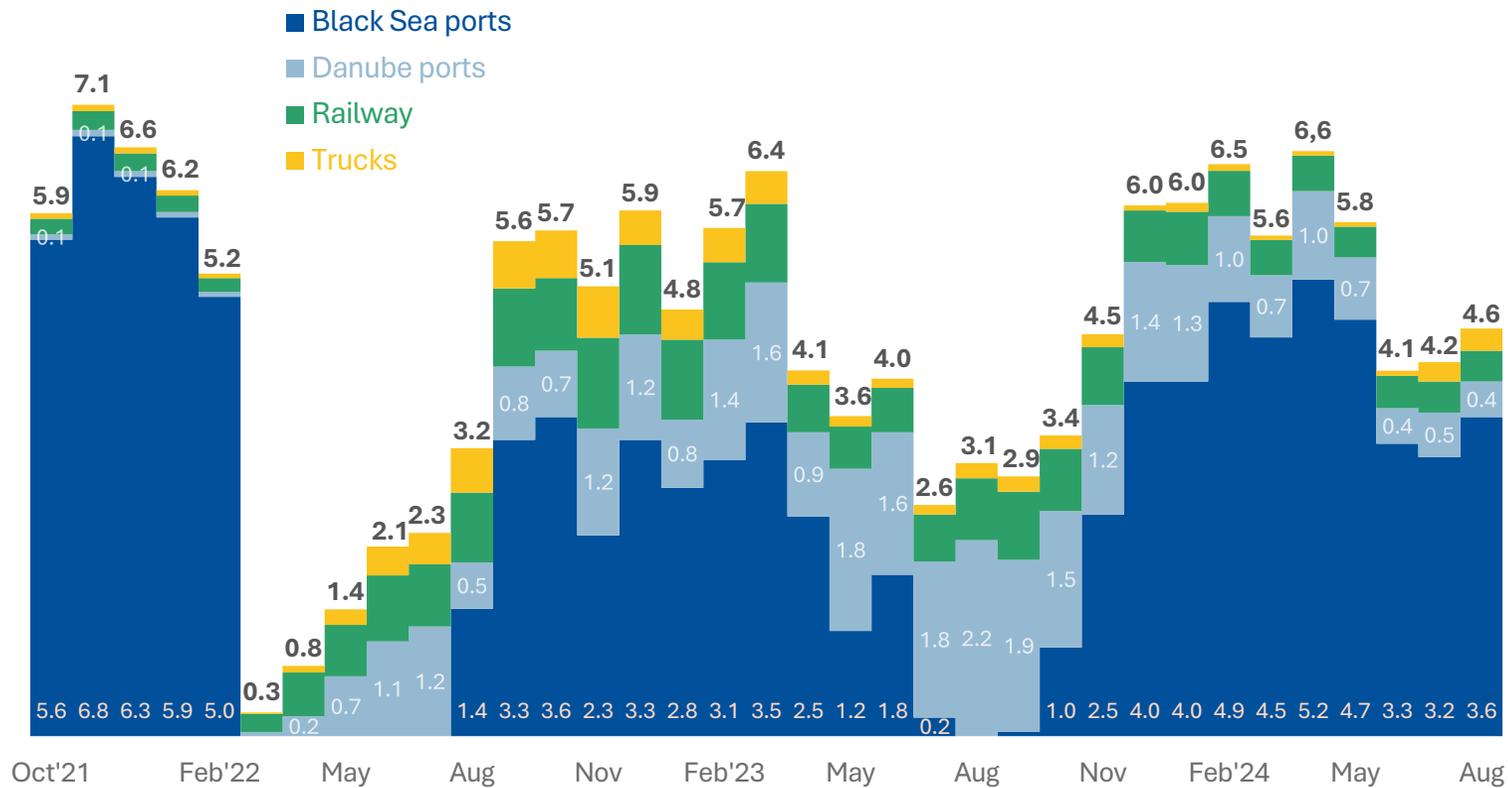
- Exports of IT services in July increased by 6% m-o-m to \$545 mn.
- Since the beginning of the year, IT exports has exceeded \$3.75 bn, down 5% y-o-y.
- The US share in service exports dropped to 36%, with the UK, Malta, and Cyprus accounting for 7-9% each.
- The total number of IT vacancies on DOU in August increased to 5421, +200 compared to July, reaching the highest figure since the beginning of the full-scale invasion.

Sources: NBU, CES calculations

SECTORAL ANALYSIS

Agricultural exports grow seasonally with the start of new crop exports

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



- In August, **agricultural exports grew by 9%** to 4.6 mt. The growth is seasonal and is driven by the increased exports of this year's crops.
- In monetary terms, in 7m2024 **total exports of agricultural and food products exceeded \$14.1 bn** and accounted for 63% of total merchandise exports.
- **The share of Black Sea ports** in exports this August **was 78%**, with another 5.4% exported by road, the highest number in last 11 months.
- **The agricultural land market in Ukraine has increased by over 30%** since the beginning of the year. In July 2024, farmland prices resumed growth after a slight decline in May-June and were the highest on record.
- **Ukraine has ratified a duty-free trade agreement with the United Kingdom.** By 2029, all import duties and tariff quotas in bilateral trade will be eliminated. Since the beginning of the year, the main export commodities to the UK have been agricultural products, namely sunflower oil, chicken meat, rapeseed and corn.

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



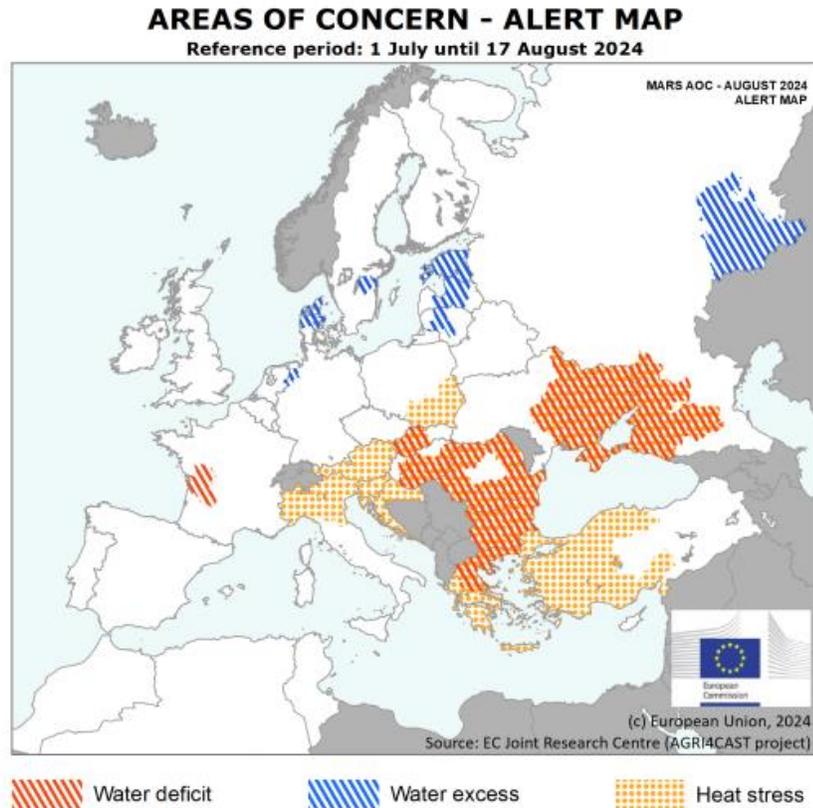
DROUGHT AND WAR: WHAT WILL BE THE HARVEST THIS YEAR?

a special topic by Natalia Shpygotska, Senior Analyst at Dragon Capital

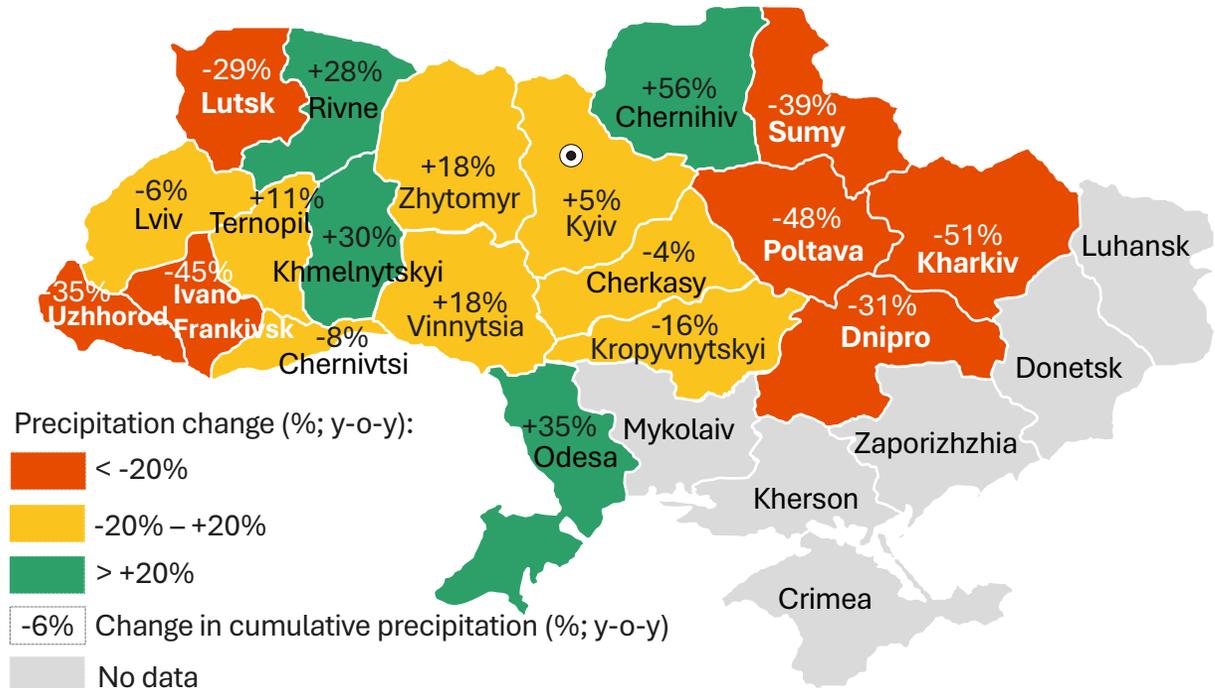
IMPACT OF WEATHER CONDITIONS ON CROP PROSPECTS FOR 2024

After three years of favourable weather conditions, Ukraine faced heat and drought in 2024

In addition to the new temperature records, cumulative precipitation in the first 8 months of 2024 decreased by 6% compared to the same period last year. However, the effect of the drought was not uniform, affecting mainly the eastern and southern regions.



Cumulative precipitation for 8 months of 2024 (change vs. 8M23; %)



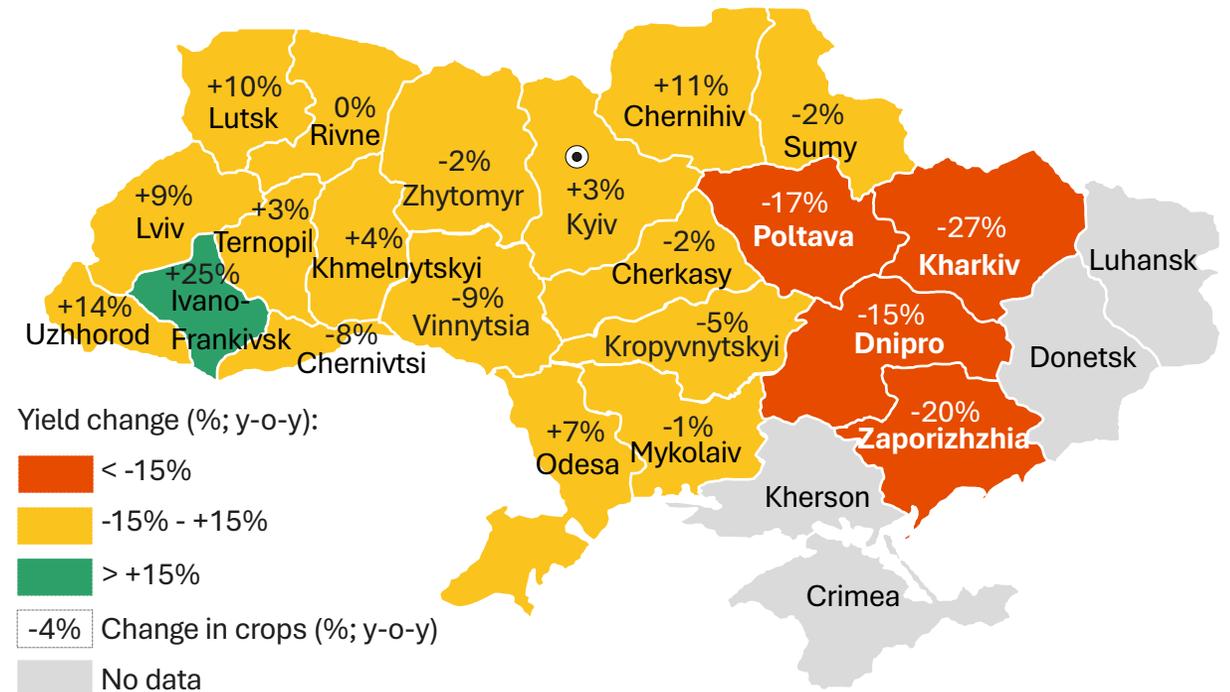
Source: Meteopost, Dragon Capital estimates

EARLY GRAIN CROPS HARVEST

Harvest of early grains and oilseeds declined only slightly in 2024

- Given the changes in planted areas and the impact of weather conditions in late 2023 on winter crop yields, the harvest of early grains and oilseeds in 2024 declined only slightly.
- The wheat harvest decreased by only 1% compared to 2023, to 22.9 Mt, with an average yield of 4.45 t/ha (-6% y-o-y)
- Barley harvest decreased by 7% compared to 2023, to 5.5 Mt, with an average yield of 3.88 t/ha (unchanged y-o-y)
- Rapeseed harvest decreased by 15% compared to 2023 to 3.4 Mt, with an average yield of 2.70 t/ha (-6% y-o-y)

Yield dynamics of early grain crops in 2024 (y-o-y; %)



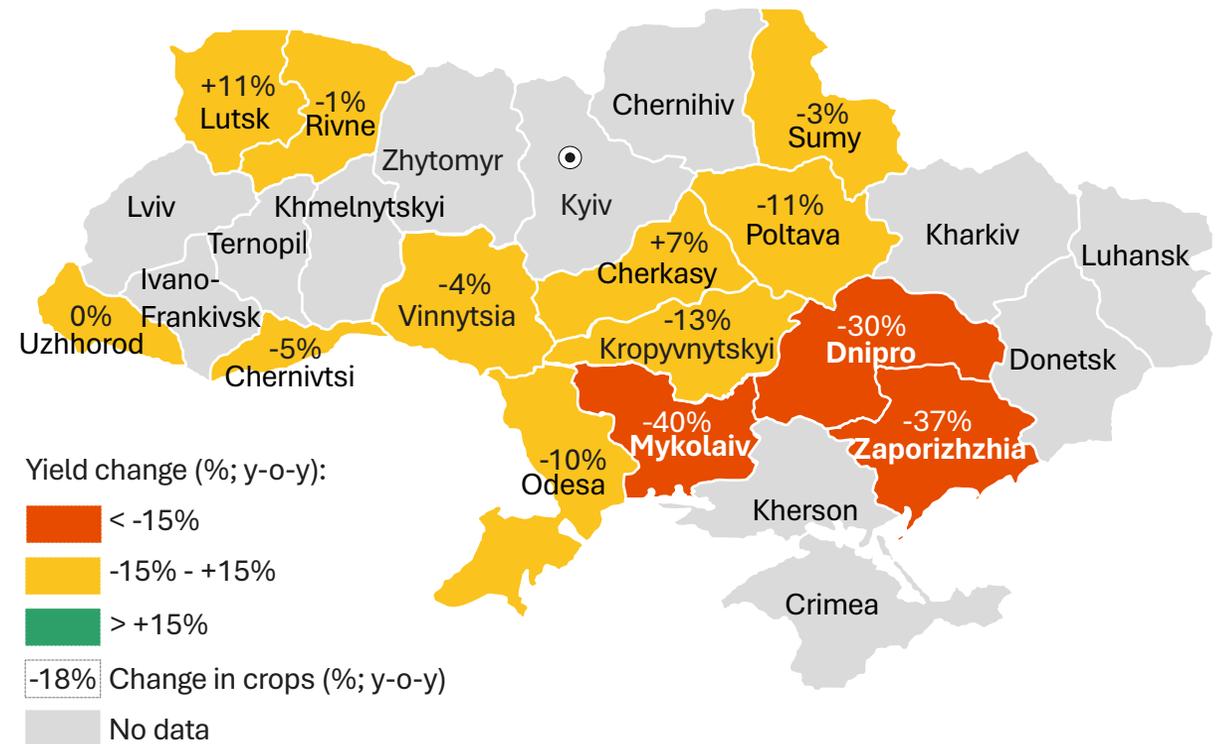
Source: Ministry of Agriculture

HARVEST OUTLOOK FOR LATE CROPS

The drought will have a significant impact of the late grains and oilseeds

- At the same time, the drought will have a much more significant impact on the yields of late grains and oilseeds, primarily corn, sunflower and soybeans
- As of the beginning of September 2024, farmers started harvesting late crops, having threshed about 20% of soybean, 15% of sunflower and less than 5% of corn.
- Based on early harvesting results, the current soybean yield is down about 25% compared to the same indicator at the beginning of the 2023 harvesting campaign, to 1.9 t/ha. The current sunflower yield decreased by 18% to 1.8 t/ha.
- Late crop yields may improve as the harvesting campaign progresses in the central and northern regions but are likely to remain below last year's figures.

Dynamics of sunflower yield in 2024 (y-o-y; %)

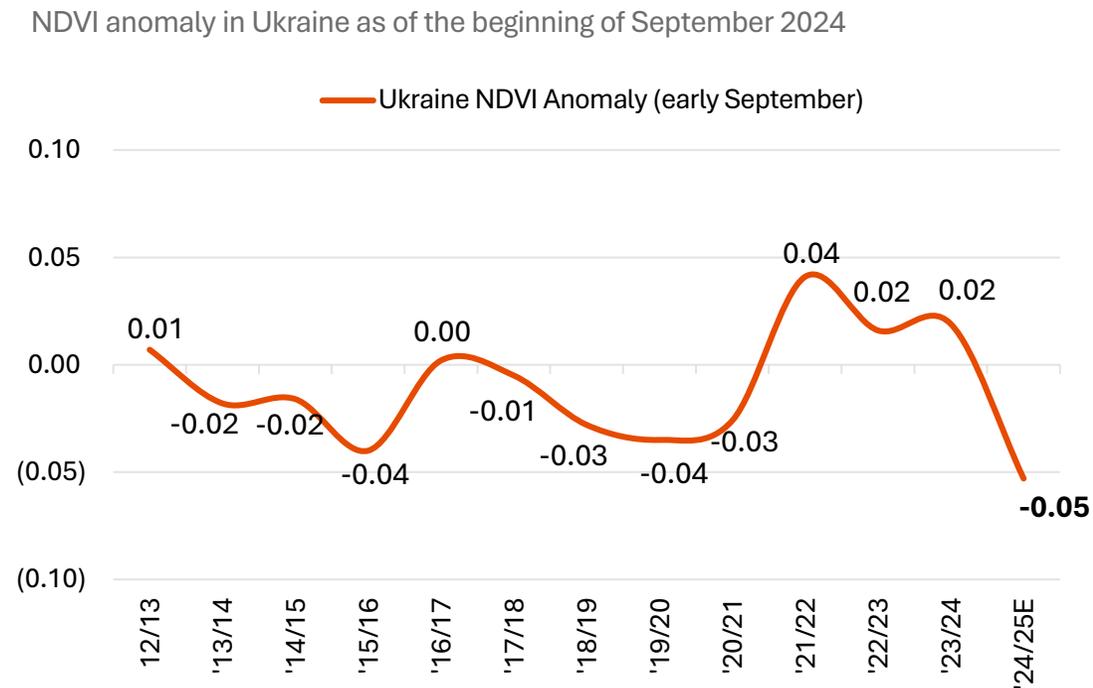


Source: Ministry of Agriculture

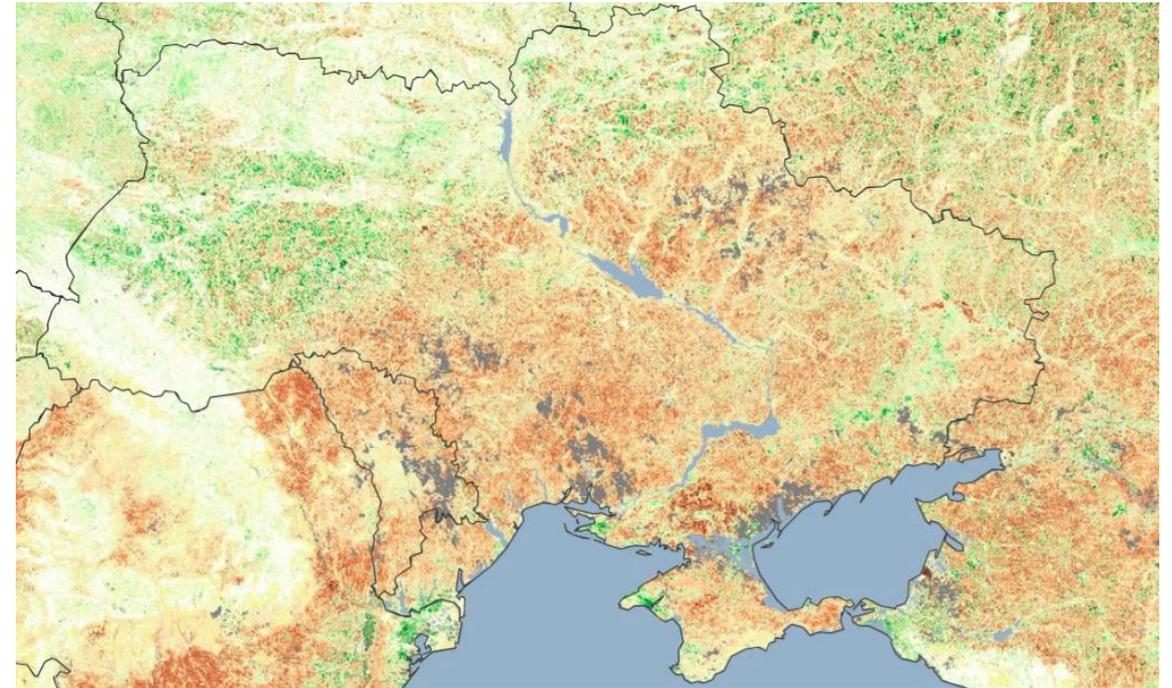
HARVEST OUTLOOK FOR LATE CROPS

Normalized difference vegetation index worst in 12 years

- Additionally, the dynamics of NDVI can help to assess the prospects for late crops in Ukraine. As of early September 2024, the **worst negative anomaly of NDVI was observed for the previous 12 years, which may indicate the prospects of a considerable deterioration in late crop yields in 2024**. The final yield will also be affected by weather conditions during September-November 2024



Source: USDA



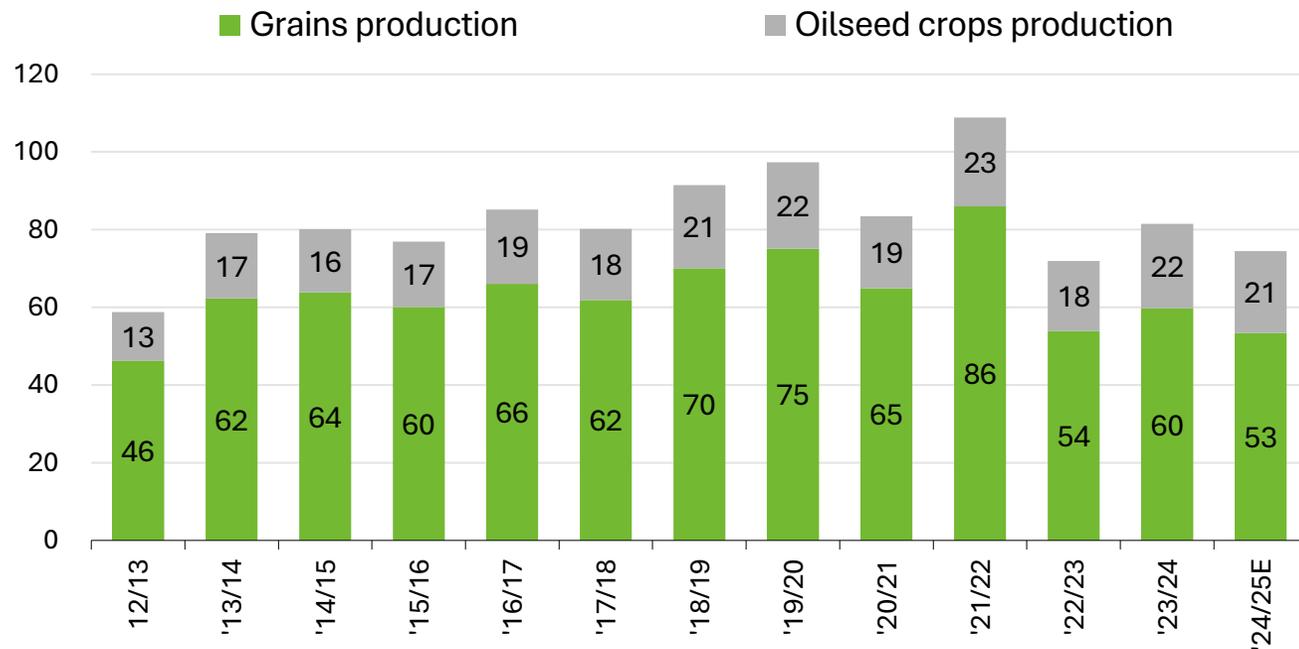
Source: USDA



PROSPECTS FOR THE 2024 HARVEST

Grain and oilseeds harvest expected to decline by 10%

Considering the preliminary results of the early grains harvesting and the prospects for a deterioration in the yields of later crops (corn, sunflower and soybeans), we expect the total grain and oilseeds harvest in Ukraine in 2024 to decline by 10% compared to 2023, to 74 Mt.



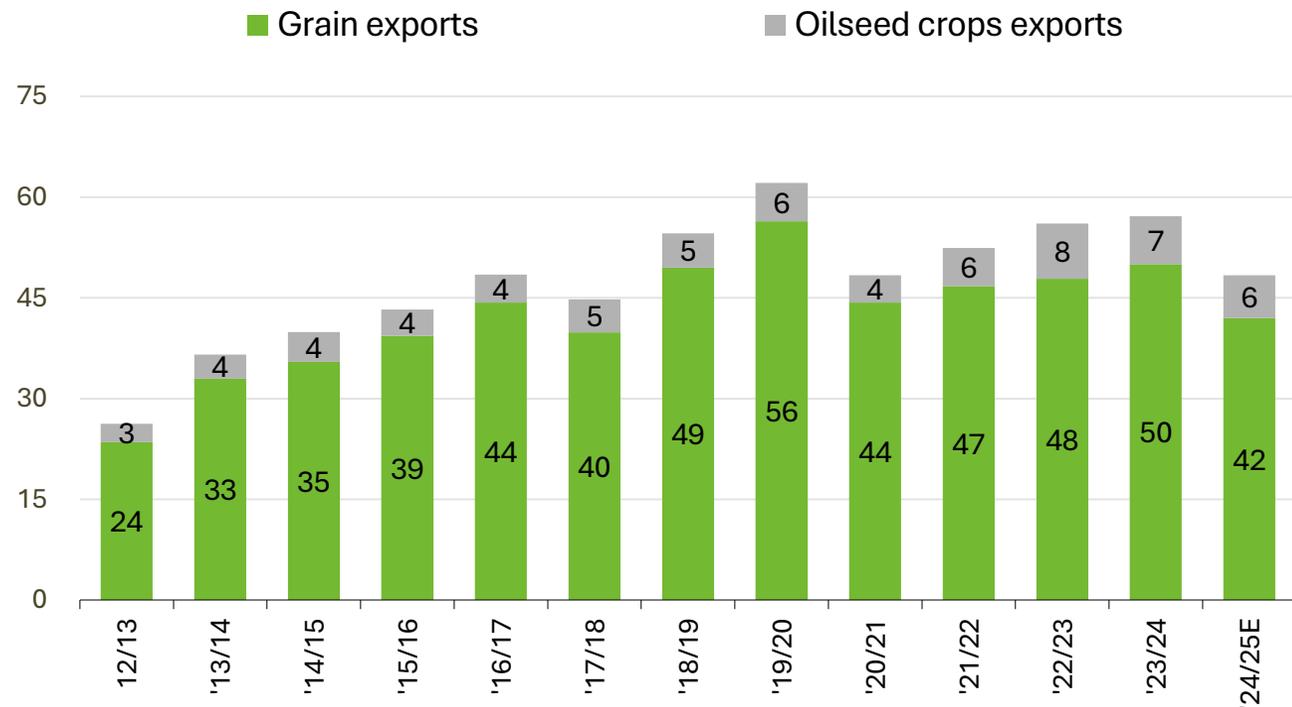
Source: State Statistics Service of Ukraine, Dragon Capital estimates



EXPORT PROSPECTS FOR 2024/25 MY

Exports of grains and oilseeds may decline by 12-15%

Given the expected decline in grain and oilseeds harvest in 2024 and the normalization of the carry-over grain stocks at the beginning of the season to pre-war levels (5-8 Mt vs. 15 Mt at the beginning of 2023/24 marketing year), exports of grains and oilseeds in 2024/25 MY may decline by 12-15%, to 48-50 Mt

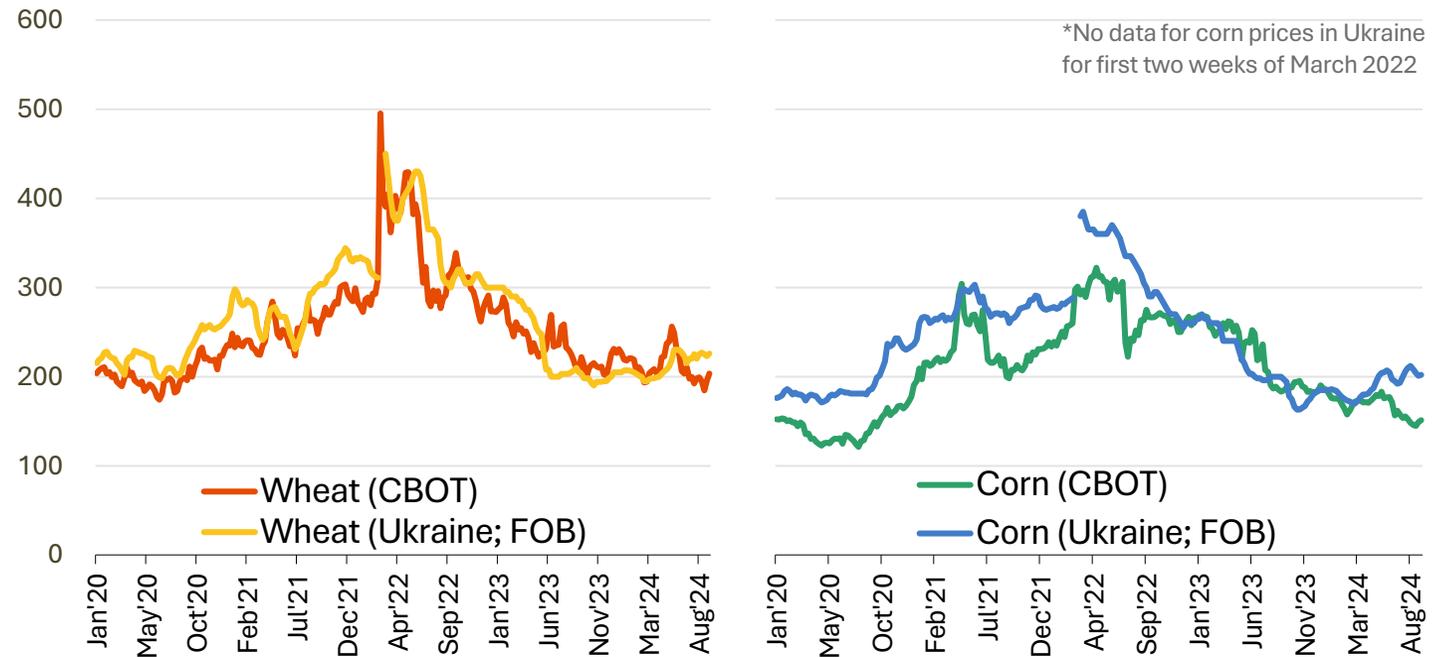


Source: State Customs Service of Ukraine, Dragon Capital estimates

OTHER FACTORS THAT WILL INFLUENCE THE DYNAMICS OF GRAIN EXPORTS:

- Stability of the deepwater ports of Ukraine
- Dynamics of prices for grains and oilseeds on world markets
- Introduction of the export guarantee regime and minimum export prices for grain

Wheat and corn prices: Ukraine versus international markets (\$/t)



Source: Bloomberg, APK Inform



THANK YOU.

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