

May 2015

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Executive Summary

- ❖ International observers (including the OSCE) and Ukrainian authorities recently reported that the Minsk II ceasefire is not being observed by Russian-backed militants, with the situation in Ukraine's East becoming more fragile. The leaders of these militants recently stated that their aim is to control the entire Donetsk and Lugansk regions.
- ❖ However, many observers now believe that Russia may have postponed or even abandoned its plans to invade the rest of Ukraine and create a "Novorossiya" state covering eastern and southern Ukraine.
- ❖ A frozen conflict could still provide the opportunity for the rest of the country to restart investments and economic growth, provided that Ukraine implements major reforms and sees improvements in its business environment.
- ❖ The Ukrainian government has started implementation of major structural economic reforms agreed upon with the IMF Extended Fund Facility, and there is agreement on the need to accelerate reform implementation.
- ❖ During January-April 2015, GDP declined by 17.6% yoy, a deeper decline than anticipated. The construction sector was the most affected, with a decline of 34.2% yoy. Industrial output dropped by 21.5% yoy in January-April (compared to 21.4% in January-March), and with major declines in Eastern Ukraine. Given these results, GDP is now expected to decline by 9% in 2015.
- ❖ The consolidated fiscal budget improved in January-April 2015, with the fiscal budget showing a surplus. This improvement was due to temporary factors as the Hryvnia devaluation and inflation which helped to increase government revenues while expenditures were controlled by austerity measures. For 2015, a fiscal deficit of 7.5% of GDP is still expected.
- ❖ The upward trend of consumer inflation continued in April 2015, with consumer prices reaching 60.9% yoy in April, compared to 45.8% yoy during March. This increase in inflation was caused principally by a large increase in natural gas tariffs for households as agreed with the IMF. Inflation by the end of 2015 is now expected to reach 45%.
- ❖ The banking sector had positive developments in April. Banks still generated losses but significantly lower than those in previous months. At the same time, there were improvements in the dynamics of both banking deposits and loans.
- ❖ The Hryvnia exchange rate stabilized at around 23 UAH/USD and is expected to remain around 25 UAH/USD during 2015, provided that the IMF program is on track.
- ❖ Ukraine's balance of payments is improving, with a current account surplus during January-April 2015, but with a larger deficit in the financial account. The overall balance of payments deficit and payments to the IMF were financed by a decline in international reserves, which reached USD 9.6 billion at the end of April.
- ❖ The Ukrainian government expects to reach an agreement with foreign creditors on Eurobond restructuring during June. The IMF is expected to disburse USD 1.7 billion in June.

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Forecast of Main Macroeconomic Indicators for 2014-2015	2011	2012	2013	2014	2015f
GDP, \$ billion	163.4	176.6	182.0	127.4	77.2
Real GDP Growth, % yoy	5.2	0.2	0.0	-6.8	-9.0
Private Consumption, real growth, % yoy	15.0	11.7	7.8	-9.6	-8.0
Fiscal Balance, incl. Naftogaz and Pension Fund, % of GDP	-4.3	-6.0	-6.5	-11.7	-7.5
Public Debt, % of GDP	36.3	36.6	40.5	72.0	94.0
Consumer Inflation, eop, % yoy	4.6	-0.2	0.5	24.9	45.0
Hryvnia Exchange Rate per USD, eop	8.0	8.0	8.0	15.8	25.0
Current Account Balance, % of GDP	-6.3	-8.1	-9.0	-4.1	0.0
FDI (\$ billion)	7.0	6.6	3.3	0.2	0.5
International Reserves (\$ billion)	31.8	24.5	20.4	7.5	13.0
External Debt (\$ billion)	126.2	135.1	142.5	135.0	153.0

Political and Reform Developments

Both international observers (including the OSCE) and Ukrainian authorities continue their close monitoring of the military situation in Ukraine along the line of ceasefire in the Donetsk and Lugansk regions. They recently reported that the ceasefire is not being observed by Russia's backed militants, with the situation in Ukraine's East becoming more fragile. The leaders of these militants recently stated that their aim is to control the entire Donetsk and Lugansk regions. On the other hand, the number of terroristic attacks in other parts of the country has declined. The emphasis is now on measures to avoid further deterioration. Also, Ukraine continues to use the ceasefire agreement to free those Ukrainian militants who are currently imprisoned by rebels. Many observers now believe that Russia may have postponed or even abandoned its plans to invade the rest of Ukraine and create a "Novorossiya" state covering eastern and southern Ukraine. If this assumption were to hold, the currently occupied territory would remain "frozen", along the lines of the territories of Transnistria, Abkhazia or South Ossetia. A frozen conflict would not be accepted by most Ukrainians, but it could still provide the opportunity for the rest of the country to restart investments and economic growth. However, this will require major improvements in Ukraine's business environment.

There are a number of reasons why Ukraine may succeed in improving its business environment. First, the government has already approved a sound economic reform agenda, a program that has been endorsed by the international community and is subject to periodic reviews by the IMF. Second, the political events in 2014 and the subsequent elections have given the current government and the President a strong mandate to implement reforms, with a strong pro-European majority in Parliament. Third, a strong civil society has emerged in Ukraine, which along with the international community, will put pressure on the authorities to deliver the reform agenda. And fourth, the government has already taken a number of initial reform measures. In fact, in the fight against corruption, an anti-corruption agency has been established and its managers appointed. Several criminal investigations against top officials on suspicion of corruption were launched in May, including several members of Parliament and top government executives. Fiscal measures are succeeding in balancing the country's fiscal budget deficits, particularly by reducing subsidies on gas consumption and restructuring the government's large external debt. At the same time, it is developing a social protection system to protect the most vulnerable groups of the population. Also, the draft law on business deregulation is under discussion by Parliamentary committees, which should significantly improve Ukraine's business environment.

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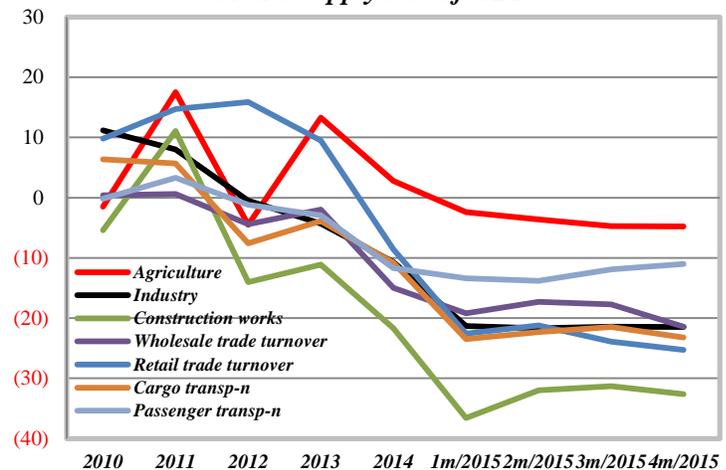
If implemented, the country's rating in the World Bank's Doing Business Report should improve. Ukraine has also announced an ambitious privatization agenda of more than 300 state-owned companies, although the number of state properties that will eventually be included in the privatization plan may be limited to several dozen.

Nevertheless, despite the fact that Ukraine is making progress in its reform agenda, this process is considered by international observers to be on "a low speed track". The Hague Centre for Strategic Studies recently said the "Soviet system is still very visible, large bureaucracy, corruption, inefficient mechanisms, obsession with laws that are supposed to change, etc." Similarly, many European leaders have recently stated that Ukraine must accelerate reforms to reach a critical mass, including reforms in public administration and civil service, reforms in election and judicial systems, constitutional reforms in the prosecution system, business liberalization, etc. All these reforms are needed to accelerate foreign investments and revive growth.

Economic Growth

During the first quarter of 2015, real GDP contracted by 17.6% yoy, a higher drop than previously anticipated. It continued the accelerated deterioration experienced during 2014, when GDP fell by 1.2% yoy in the first quarter, 4.5% yoy in the second quarter, 5.4% yoy in the third quarter, and 14.8% yoy in the fourth quarter. As stated in previous monthly reports, these declines in economic activity were mainly a result of the hostilities caused by Russian-backed militants in the East, which affected exports to Russia and other countries, impaired infrastructure and productive facilities in the industrial center of the country, and led to inflation and currency depreciations.

Economic Performance of Ukraine, % yoy
On the supply side of GDP



Source: State Statistical Service of Ukraine, The Bleyzer Foundation

Monthly production statistics in 2015

suggest that private consumption may have experienced a sharp decline. In fact, during January-April 2015, retail trade declined by 25.3% yoy. Private consumption may have also been affected by the decline of real wages in Ukraine of 29.6% in April 2015, compared to April 2014. During the first quarter of 2015, capital investments also declined, with a drop of 14.8% yoy (compared to a decline of 24.1% during the entire year 2014). The most affected sectors by declines in capital investments were the finance/insurance sector (-43.8% yoy), industry (-37.4% yoy) and wholesale and retail trade (-35.8%). Region-wise, the highest declines in capital investments took place in Lugansk (-94.1% yoy) and in Donetsk (-70.9% yoy), while capital investments in Volyn increased by 67% yoy, and in Kyiv by 32% yoy.

On the supply side of GDP, in January-April 2015, the most affected sectors were construction (with a decline of 32.6% yoy) and retail trade (-25.3% yoy). During this period, industrial production declined by 21.5% yoy, compared to 21.4% yoy in January-March 2015. Major industrial output declines during January-April took place in coke and oil refining (-43.6% yoy), metallurgy (-25.7% yoy) and machinery and equipment (25.8% yoy), all sectors affected by the hostilities in the East. In fact, region-wise, during January-April 2015 the largest declines in industrial production took place in Lugansk (-88.0% yoy), Donetsk (-51.7% yoy), Kirovohrad (-23.2% yoy), and Kharkiv (-17.5% yoy). On the other hand, positive rates of industrial output were shown in Vinnytsya (14.0 % yoy), Rivne (9.7% yoy), Chernivtsi (7.7% yoy), and Volyn (7.6% yoy).

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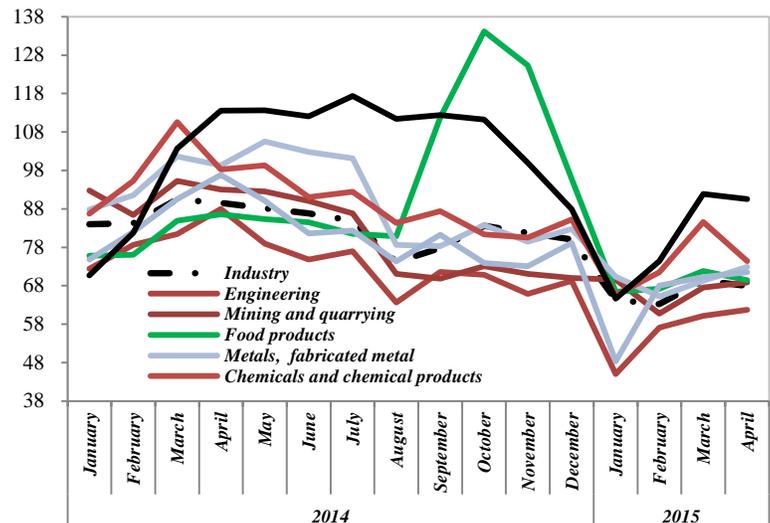
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As in previous years, agriculture was the best performing sector with the lowest decline (-4.8% yoy during January-April). Nevertheless, in the marketing year July 2014/June 2015, grain production is expected to reach 63 million tons (compared to 64 million tons in 2013/14). In this marketing year, grain exports will reach about 32 million tons, an amount similar to last year, making Ukraine the world's second largest grain exporter after the US, according to USDA statistics.

Although the recent declines in GDP have been sharp, the impact on the population has been cushioned by three factors. First, Ukraine's informal economy has expanded substantially since the beginning of 2014, providing unreported income to the population. A recent study by the Ministry of Economy shows that the informal economy may have increased from about 35% of GDP in 2013 to about 42% of GDP in 2014, the highest level since 2007. This increase was induced by the military conflict, weaknesses in the banking sector, and currency inflation and depreciation. Second, the population has been using its substantial foreign exchange savings to maintain current consumption, as demonstrated by the fact that foreign exchange sales by the population have exceeded purchases for several months in a row, and foreign currency deposits in April 2015 declined by 35.4 % yoy. Third, the significant transfers of funds from abroad, principally to relatives in Ukraine, have helped ameliorate the effects of GDP declines on living standards. In fact, according to NBU statistics, net current transfers in January-April 2015 reached USD 629 million, compared to USD 1,541 million in 2014.

Index of Industrial Production in Ukraine for 2014- 2015,
Dec 2013 = 100



Source: State Statistical Service of Ukraine, The Bleyzer Foundation

During the second half of 2015, GDP is not expected to contract as sharply as in the first half for a number of reasons. First, the major source of GDP contraction (export declines to Russia) has been exhausted with exports to Russia becoming negligible. Second, major declines in GDP took place in the second half of 2014, which will provide a low statistical base for the second half of this year. Third, consumer and investor confidence is growing as there are indications that the hostilities in the East may be frozen, without expanding into the rest of the country. Fourth, it is quite likely that the negotiations on debt restructuring will be completed by June, enabling the disbursement of IMF funds. And finally, the banking sector is being rehabilitated, thanks to strong actions by the NBU. As a result of these factors, GDP is expected to fall in 2015 by 9.0%, a lower rate than in early 2015. If these positive factors are maintained, we expect that GDP will start recovering in early 2016.

Fiscal Policy

During the first quarter of 2015, the consolidated fiscal budget was in surplus thanks to temporary factors that are unlikely to hold in the rest of the year. In this period, the growth in fiscal revenues compared to expenditures generated a surplus of almost UAH 14 billion. Updated data on the execution of the consolidated budget showed that this favorable outcome was helped by both inflation and Hryvnia depreciation. This favorable impact outweighed the fact that economic output and retail trade diminished during January-April 2015.

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But the impact of Hryvnia depreciation slightly diminished as the UAH/USD exchange rate appreciated to around 23.5 UAH/USD in March. Overall, the growth rate of consolidated budget revenues increased by more than 2.5 times to 25% yoy in January-March compared to January-February. Growth of consolidated budget expenditures almost doubled but remained significantly lower than that of revenues at 12.7% yoy.

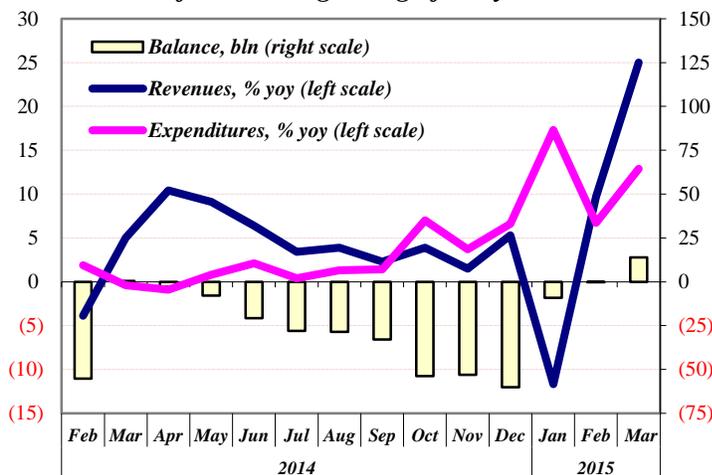
A closer look at consolidated budget revenues shows that receipts are growing faster at the state level than at the local level. Revenues of the state budget alone grew by 27.5% yoy. Same as in January-February 2015, the highest contributions to the general fund of the state budget revenues were made by taxes and charges, which to a great extent are influenced by inflation and national currency depreciation. In particular, receipts from VAT on imported goods amounted to UAH 29.9 billion, which is a 71.9% yoy increase. Receipts from the VAT on domestic goods totaled UAH 25.1 billion. This was a 32.1% yoy increase, which is significantly higher than the 1.8% yoy growth observed in January-February.

The mentioned growth may reflect the statistical base effect (growth of the corresponding VAT receipts reversed the trend to a 10.4% yoy decline in January-March 2014 from a 2.4% yoy increase in January-February) and the effect of accelerated inflation. At the same time, receipts from corporate profit taxes saw a significant deceleration in decline in January-March 2015. These tax receipts posted a 3.6% yoy decline to UAH 14.9 billion over the period, compared a 36.4% yoy decline in January-February 2015. This deceleration took place even though large and medium enterprises saw an increase in losses by 3.1 times in Q1 2015 compared to the corresponding period of 2014. One of the causes for the improvements in receipts from the VAT and corporate profit tax is the significant improvement in collection of receipts thanks to reforms of the tax authorities.

However, complaints from business entities show that reform is far from being successful as tax collection procedures are still cumbersome and complicated. The second explanation for growth in corporate tax receipts may be application of an advance payments scheme. This practice has been extensively used by previous governments to cover cash gaps. However, it has no justification in the current situation when the state budget revenues are significantly higher than expenditures. The third explanation may be application of another practice in tax receipts collection, which was extensively used previously. That is the scheme under which tax authorities determined the size of tax payments for large enterprises by way of negotiations with their owners/oligarchs. If this is the case, then it seems that the oligarchs have agreed to pay higher tax contributions than last year when the situation with their companies' profits was not as harsh as it is now (according to official statistics). This is possible only if the actual situation with profits is much better than that reported to the State Statistics Service thanks to operations in shadow economy.

Similar to budget revenues, total government expenditures also grew faster at the state level than at the local level as state budget expenditures posted a 20.3% yoy increase in Q1 2015. Classification of expenditures by purpose shows that most of the state budget expenditures observed either accelerated growth or decelerated decline during the reporting period. The acceleration of growth in the case of expenditures for defense, public order, security, and judiciary was related to continued unrest in Eastern Ukraine. The introduction of austerity measures was reflected by lower state budget expenditures on economic activity by 15.6% yoy, general public functions by 7.7% yoy (even though they increased at the local level), education by 4.3% yoy, and social security by 2.4% yoy.

Dynamics of consolidated fiscal budget components from the beginning of the year



Source: The Ministry of Finance of Ukraine, The Bleyzer Foundation

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Continued reform of the healthcare system was accompanied by a redistribution of budget expenditures in favor of local budgets. In particular, the state budget for healthcare expenditures declined by one-fifth to UAH 1.4 billion in year-over-year terms, while healthcare expenditures from the local budget grew by 31.2% yoy to UAH 13.7 billion. Amendments to budget legislation were also adopted to transfer additional expenditures of UAH 2.9 billion to local budgets to repay arrears on compensation for the difference between existing tariffs and the actual cost of provided services. But these funds were not distributed because procedures for their utilization have been not adopted yet. As a result, housing and utilities expenditures continued to decline at a high annual rate.

In April 2015, the growth of consolidated budget revenues continued to outpace growth of expenditures. According to preliminary estimates, the consolidated budget revenues totaled UAH 198.409 billion as of April 30th, which is a 30.5% yoy increase. At the same time, consolidated budget expenditures expanded by 15.5% yoy to UAH 178.76 billion. Therefore, the consolidated budget surplus further increased to UAH 18.493 billion from UAH 13.971 billion observed at the end of March. Nevertheless, it is expected that during the rest of 2015, expenditures will outpace revenues, particularly due to higher military expenses and the need to provide social support to the population affected by high utility tariff increases. As a result the consolidated fiscal budget is expected to show a deficit of 7.5% of GDP, including funding of the deficits of Naftogaz and the pension fund.

Monetary Policy

Inflation. Consumer inflation further accelerated in April 2015 to 60.9% yoy (compared to 45.8% yoy in March), on the back of housing and utilities tariffs, which increased by 188% yoy. Nevertheless, most of the major consumer price indices observed acceleration in growth during the month. A minor deceleration in growth of prices of foods (from 52.7% yoy to 52.3% yoy) was fully offset by acceleration in prices of non-alcoholic beverages (by 11.3 percentage points to 76.8% yoy). Also in April, the government significantly raised electricity and gas tariffs. As a result, growth in electricity prices accelerated from 11.3% yoy in March to 48.7% yoy. At the same time, prices of town gas and natural gas grew by 9 times yoy in April, pushing growth of total housing and utilities prices from 37.7% yoy observed in March to 188.2% yoy. Slower growth in prices was observed in transport (from 65.5% yoy in March to 43.8% yoy in April), healthcare (from 48.4% yoy to 45.8% yoy), and recreation and culture (from 47.4% yoy to 46.5% yoy). Growth in prices of communication services remained virtually unchanged (at 5.5% yoy).

We expect consumer inflation to go down to around 45.0% by the end of 2015. This is because the major increase in housing and utilities tariffs already took place in April and its impact on total consumer inflation will diminish with time. The planned increases in prices of cold water and sewerage and at least one more increase in electricity tariffs will have a less significant impact on consumer prices in total. At the same time, consumers will cut their purchases of durables due to higher payments for housing and utilities. In addition, the NBU will continue transferring its monetary policy to inflation targeting in full compliance with obligations to the IMF.

Banking Sector. The banking sector of Ukraine observed some positive developments in April. Banks still generated losses but significantly lower than those of previous months. At the same time, there were improvements in the dynamics of both banking deposits and loans.

Stabilization on the foreign exchange market and NBU measures to stabilize the banking system in general brought the first positive results in April. The buildup of losses significantly decelerated during the month thanks to both lower losses of insolvent banks under administration and the first profits of solvent banks. In particular, solvent banks managed to generate UAH 1.9 billion in profits in April, lowering losses accumulated from the beginning of the year to UAH 14.3 billion. Insolvent banks generated just around UAH 4 billion of losses during the reporting month compared to an average of over UAH 21 billion per month during Q1 2015.

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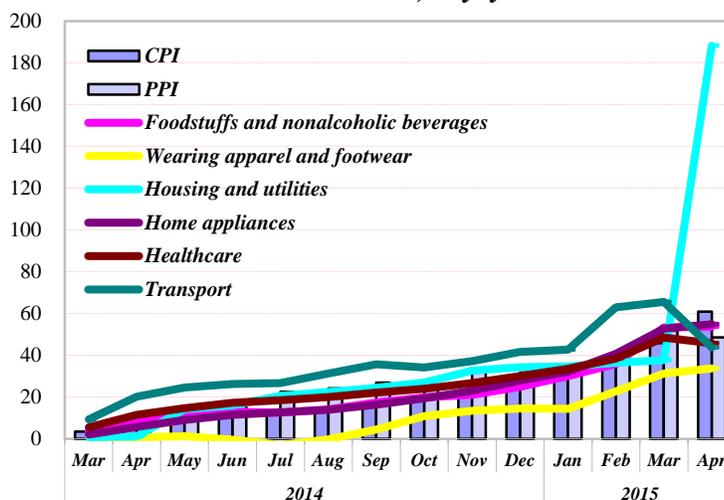
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As mentioned in our previous report, the bank losses were the result of a high allowance for potential losses on loans. At the same time, the separation of insolvent banks out of the banking system and the stabilization on the foreign exchange market significantly slowed the buildup in loss allowances in April. In fact, allowances for potential losses on loans were at the lowest this year, at UAH 3.7 billion. On the other hand, the needs for financial assistance from the NBU remained high among banks. The regulator provided UAH 13.38 billion to support the liquidity of 13 banks in April, which is comparable to the amount provided in March, even though the number of banks requesting assistance almost halved. Overnight loans were provided to 8 banks for the amount of UAH 8.526 billion. Eight banks received loans with maturity of up to 90/360 days in the amount of UAH 1.715 billion. Just 2 banks applied for and received loans under the financial rehabilitation program, but one of them (same as in March) was the largest bank of Ukraine, Privatbank. UAH 1 billion was provided to one bank under direct repo transactions.

CPI, PPI, and Growth of Prices for Select Goods and Services, % yoy



Source: State Statistical Service of Ukraine,
 The Bleyzer Foundation

In April, the situation with banking deposits improved both in national currency and foreign currency. National currency deposits posted 0.6% mom growth, which was the first growth registered this year. In particular, increases in deposits with duration up to one year and more than two years more than offset the declines in call deposits and deposits with duration from one to two years. These developments indicate that confidence of the population is improving. From the beginning of the year, the national currency deposits of private persons continuously declined faster than deposits of businesses. In April, the situation was reversed as private persons ensured the increase in deposits, while deposits of business entities further decreased. The reverse of trend in national currency deposits in monthly terms led to further deceleration of their decline in year-over-year terms to 8.2%. As for foreign currency deposits denominated in US dollars, they saw significant deceleration in their decline in April. Overall, foreign currency deposits denominated in USD dropped 2.1% mom compared to 7.4% mom a month ago. Only deposits with a duration of more than two years posted growth, while all the other foreign currency deposits posted declines. Similar to the situation with national currency deposits, private persons drove positive changes in dynamics in foreign currency deposits. In particular, the monthly decline in the foreign currency deposits of private persons decelerated to around 2% mom, while the decline in foreign currency deposits of businesses remained above 5% mom. At the same time, the year-over-year decline in foreign currency deposits denominated in USD sustained few changes, equaling 35.4% (1.2 percentage points lower than in March yoy).

Banking loans observed some positive developments in April. Improvements were observed in national currency loans, while the decline in foreign exchange-denominated loans remained unchanged. Even though the monthly outflow of national currency loans continued, its pace decelerated five times to just 0.5% mom. The 1.9% mom growth in long-term national currency loans almost fully compensated for a 1.8% mom decline in medium-term national currency loans and just a 0.23% mom decline in short-term national currency loans. In year-over-year terms, total national currency loans dropped 11.1%, which is almost the same as in March. At the same time, the decline in foreign currency loans denominated in USD accelerated by around 4 percentage points to 30% yoy. That was the result of a faster monthly decline in correspondent loans at 9% mom on the back of negative changes in loans through all the term groups.

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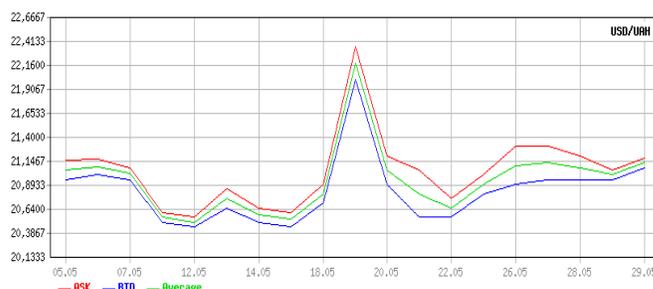
Hryvnia Exchange Rate. The NBU did not change its policy on the foreign exchange market in May. On the one hand, the regulator did not lift any of the restrictions introduced earlier to stabilize the market. On the other hand, it extensively cut the requests from banks for foreign exchange purchases on the interbank foreign exchange market. At the same time, contrary to expectations, the NBU was not active as a player on the interbank foreign exchange market in May. The regulator made several two-way interventions at the beginning of the month but the traded amounts were not very high. It also made several “verbal” interventions, announcing its target exchange rate at the beginning of the trading sessions. Starting from the second half of the month, the National Bank stopped making even “verbal” interventions.

At the same time, holidays at the beginning of the month and traditionally lower business activity in the country at the end of spring and during most part of summer were the reasons for significantly lower demand for dollars during the month. Therefore, the UAH/USD exchange rate had appreciated a bit at the beginning of May around 20.5 UAH/USD as expected. It did not sustain significant fluctuations for most of the month afterwards. The only exception was observed on May 18th, when the exchange rate depreciated by around 1.5 UAH/USD. This depreciation was related to actions of one systemic bank. The bank placed high bids for dollars to ensure

the needed purchases of foreign exchange regardless of the price after the NBU had extensively cut the bank’s requests for dollar purchases. Since the interbank foreign exchange market remains thin, such actions led to immediate Hryvnia depreciation. However, the exchange rate returned to the level observed at the end of April and is expected to remain stable in June unless there will be significant shocks to the economy.

Taking into account the very difficult negotiations on the external debt restructuring, commitments to the IMF, and hard economic conditions, we leave our forecast for the exchange rate around 25 UAH/USD in the second half of the year unchanged.

Dynamics of UAH/USD Exchange Rate Quotations in the Interbank Forex Market in May



Source: Ukrdealing, The Bleyzer Foundation

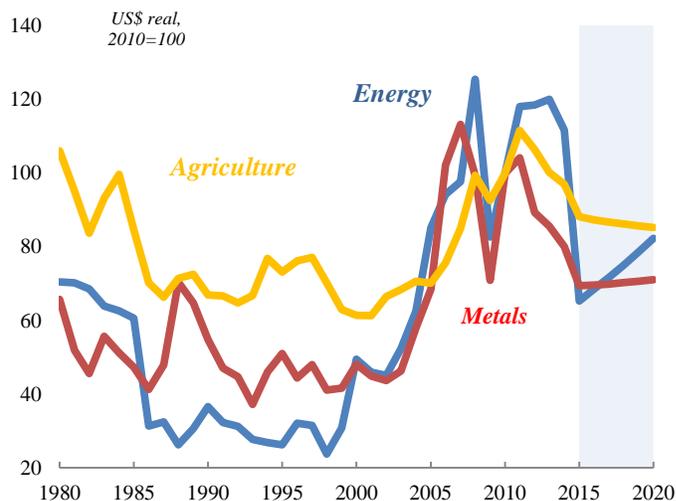
International Trade and Capital

According to NBU statistics, the current account of Ukraine’s balance-of-payments continues to improve despite lower exports. In April 2015, the current account had a surplus of USD 0.2 billion, following a similar surplus in March.

Exports of goods and services continued to decline, with a drop of 36.1 yoy in April. In April total exports amounted to USD 4,012 million. Although the major reason for the decline in exports was trade restrictions imposed by Russia, the continuous decline in world commodity prices has affected the dollar value of Ukrainian exports.

As shown in the side chart, prices of metals, agriculture and energy have declined in the last few

Commodity price indices, annual with forecast



Source: The World Bank

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May 2015

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years, with little future expected recovery, except for energy. Export declines during January-April 2015 took place in all major merchandise groups, including mineral products (-58.6% yoy), machinery and equipment (-48.3% yoy), chemicals (-34.7% yoy), metallurgy (-36.8% yoy), and agriculture (-17.0% yoy). The recovery of exports will depend crucially in the ability of Ukraine to seek new markets for its products, given the likelihood that exports to Russia will remain depressed. Ukraine will also need to diversify its export products. The Free Trade Agreement with the EU may play a key role in this export diversification.

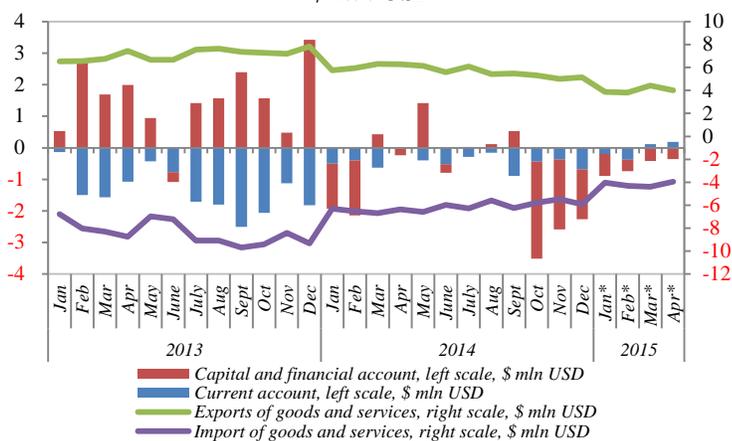
In April, imports of goods and services amounted to USD 3,941, a decline of 38.2% yoy, a slightly deeper decline than exports. The largest decline in imports of goods took place in the agricultural sector, with a decline of 48.3% yoy in January-April 2015. Imports of energy and other mineral products declined by only 15.1% yoy, but with lower imports from Russia and larger imports from the EU. Imports of machinery and equipment during January-April also registered a large drop of 43.6% yoy.

The financial account of Ukraine improved during April 2015, but still showed a deficit of USD 355 million, compared to a deficit of USD 420 million in March. Despite improvements in the financial account deficit, the possibility of low external debt rollover ratios constitutes a risk for the financial account. In fact, in April 2015, commercial banks had to make repayments of USD 348 million while the corporate sector had repayments of USD 697 million. For this reason, the ongoing negotiations on debt restructuring both for public and private external debt are critical. There are signals coming from both Ukrainian Eurobond holders and state authorities that restructuring of state debt may be completed in June. But there are still disagreements principally on the extent to which "haircuts" on principal bond amounts would be imposed. The newly adopted law on The Right of Ukrainian Cabinet of Ministers to Impose Moratorium on Payments on Commercial Debts might be interpreted as "extra pressure", which Ukraine tries to impose on its bondholders to restructure the debt with haircuts. Most analysts believe that some "haircut" may finally be agreed upon, though not as large as the government may wish. Other likely outcomes of the restructuring would include (i) a significant increase in the maturity of the bonds (up to 10 years) and (ii) a decrease in the coupon rate (by 1 to 3 pp).

It is expected that in June 2015 the IMF will be able to disburse its second tranche of about USD 1.7 billion under the EFF Program. The May 2015 IMF mission to Kyiv stated that "understandings were reached on most issues and that discussions will continue in the coming days to finalize a staff-level agreement than can be taken for approval to the IMF management and the Executive Board." On debt restructuring, although its completion is not a benchmark or disbursement condition, the IMF stated in Washington, D.C. that "it is vital that Ukraine and its creditors reach an agreement in line with the objectives stated in the Memorandum that was signed." The IMF may be concerned about debt sustainability and must be satisfied that the government's financial program is fully funded.

In April, the overall Balance of Payments had a deficit of about USD 168 million. This deficit plus repayment under the IMF loan (USD 218 million) were financed via the decline in international reserves. At the end of April, international reserves stood at USD 9.6 billion, an amount equivalent to about 2.5 months of current imports of goods and services.

Ukraine's External Balance of Payments Performance,
\$ mln USD



Source: NBU, The Bleyzer Foundation

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