



CONCORDE CAPITAL

Inflation

Stealing all the headlines this week

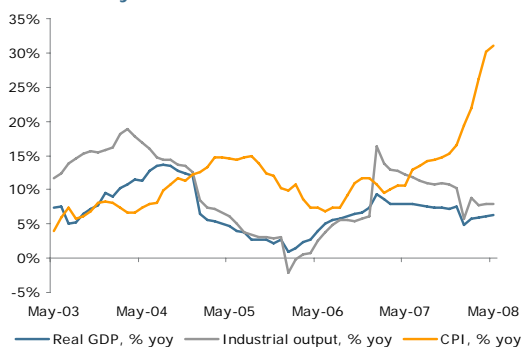
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Business cycle indicators



Source: State Statistics Committee

Key macroeconomic indicators

	2007	2008E	2009F
Real Economy			
GDP real growth, % yoy	7.6	6.8	6.5
Nominal GDP, USD bln	141.2	194.0	239.3
Industrial output growth, % yoy	10.2	8.7	7.5
CPI (eop), % yoy	16.6	21.0	15.0
PPI (eop), % yoy	23.2	33.0	18.0
Retail trade growth, %	28.8	25.5	25.0
Banking assets growth, %	76.0	50.0	45.0
Construction growth, %	15.8	20.0	25.0
External Sector			
Trade balance, % GDP	-5.6	-5.5	-5.8
Current account balance, % GDP	-4.2	-4.5	-5.3
Net FDI, USD bln	9.2	10.4	13.5
NBU reserves, USD bln	32.5	38.7	37.5
Monetary & Fiscal Policy			
Money supply, % yoy	51.7	25.0	40.0
UAH/USD (eop)	5.05	4.95	4.90
Consolidated budget, % GDP	-1.1	-1.0	-0.5

Source: State Statistics Committee, National Bank of Ukraine, Concorde Capital estimates

Prices for core commodities, as of Jun 13

	Current	%, YTD	%, yoy
Gas imports, USD/tcm	179.5	0%	38%
Crude oil (URALS), USD/bbl	130.0	41%	94%
Winter wheat, USD/mt, FOB**	292.0	14%	44%
Semi-finished steel, USD/mt, FOB**	945.0	74%	77%

**Black Sea ports

Source: Bloomberg

- Standard & Poor's downgraded Ukraine's sovereign ratings on June 12, citing authorities' lack of counteractive policies to bridle inflation
- The National Bank's June 6 inflation report, quickening GDP growth (+6.4% yoy in 5M08) and the government's 2008 macro forecast revisions two days ago (CPI to 15.3%, PPI to 24.6%) suggest that concerns of overheating have legs
- On the flipside, CPI growth slowed to 1.3% mom in May from 3.1% mom in April and PPI to 3.7% mom vs. 6.6% a month ago. We see inflationary pressure abating through year and keep our 2008 forecasts of 21.0% for CPI and 33.0% for PPI

S&P downgrades Ukraine on inflation concerns

Yesterday Standard & Poor's, in its announcement downgrading Ukraine's sovereign ratings, singled out "the failure of Ukrainian authorities to put into place adequate policy measures to counter rising inflation in Ukraine's overheating economy." Ukraine's long-term foreign currency rating was lowered from BB- to B+, the long-term local currency rating from BB to BB-.

NBU issues inflation report

A week earlier, the National Bank of Ukraine issued its first-ever special "inflation report." The report's language leaves no room for questions, saying that GDP growth was 1.7% above its sustainable level in 1Q08. As of May, real GDP growth was 6.4% yoy this year, accelerating for the fourth consecutive month. The NBU also argued that there is a probability inflation unfolds further, as Ukraine's narrow core inflation* sped up from 3.7% yoy in December 2007 to 6.2% yoy in April 2008. The report also noted that businesses' inflationary expectations are on the rise: in 1Q08, enterprises expected consumer prices to rise 15.6% in the next 12 months, vs. 11.1% in 1Q07.

Government raises its inflation forecast

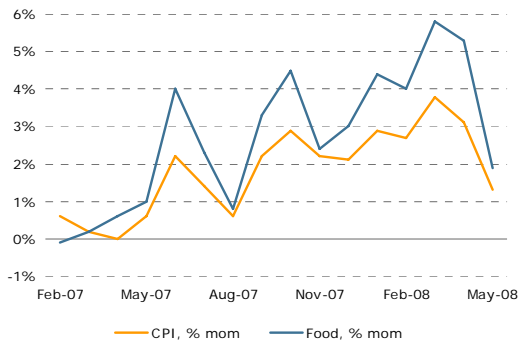
As early as March, CPI, at 9.7% YTD, beat the government's full-year projection of 9.6%. Just this week, on June 11, the Cabinet of Ministers lifted its forecast for 2008 CPI to 15.3%, and PPI from 19.2% to 24.6%, in addition to scheduling amendments to the state budget for June 17 (government forecasts are the basis for state budget projections).

Our view...

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* The NBU calculates "broad core inflation" (excluding commodities and items with low level of processing) and "narrow core inflation" (excluding food and energy prices).

CPI and food prices



Source: State Statistics Committee

Our view

The government's revised forecasts look unrealistic, and we believe could be overly optimistic for political reasons. Consumer inflation reached 14.6% YTD (+31.1% yoy) in May, close to the government's full-year forecast of 15.3%. The same holds true for PPI, which hit 24.2% YTD (+39.4% yoy) in May.

Nevertheless, we believe inflationary pressure will ease in the second half of the year, and retain our forecasts unchanged: CPI of 21.0% yoy and PPI of 33.0% yoy in 2008. We contend that domestic food prices will stop their upward trend this summer and may even deflate slightly, on the back of an expected plentiful harvest.

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