



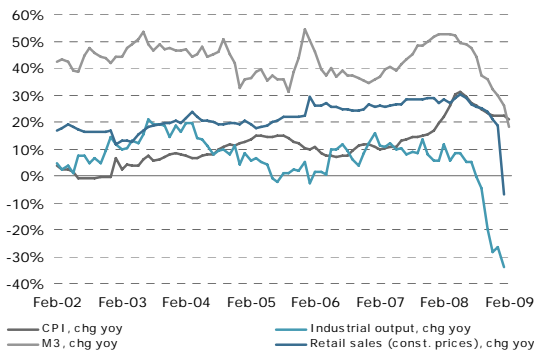
# IMF stabilization loan

Back on track

March 12, 2009

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## Economic snapshot



Source: State Statistics Committee

## Key macroeconomic indicators

	2007	2008	2009E
<b>Business cycle</b>			
Real GDP, chg yoy	7.6	2.1	-7.0
Nominal GDP, USD bln *	141.2	180.4	119.5
Industrial output, chg yoy	10.2	-3.1	-11.5
CPI (eop), chg yoy	16.6	22.3	15.0
PPI (eop), chg yoy	23.3	23.0	18.0

## External sector

NBU reserves (eop), USD bln	32.5	31.5	23.3
FDI net, USD bln	9.2	9.9	7.5
C/A balance, % GDP	-4.2	-6.6	-1.1
Trade balance, % GDP	-5.6	-7.6	-1.9
External debt, % of GDP *	58.6	60.7	78.9

## Exchange rate

Interbank UAH/USD (avg)	5.03	5.27	8.50
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Source: State Statistics Committee, National Bank of Ukraine, Ministry of Finance, Bloomberg, Concorde Capital estimates

## Prices for core commodities, as of March 12

	Current	%, YTD	%, yoy
Gas imports, USD/tcm	360.00	0%	101%
Crude oil (URALS), USD/bbl	40.77	-3%	-60%
Milling wheat 3rd gr, USD/mt, FOB**	153.00	24%	-44%
Steel square billet, USD/mt, FOB**	295.00	-19%	-63%

\*\*Black Sea ports

Source: Gas of Ukraine, Bloomberg

- Yesterday, Ukrainian authorities acceded on compliance with the IMF requirements on the extension of the 2nd tranche of the USD 16.5 bln loan
- The IMF confirmed that Ukraine will receive the 2<sup>nd</sup> tranche but the timing is not clear yet
- CDS on Ukraine's 5y sovereign bonds shed 709 bps over the last two days; today the hryvnya appreciated 4.9% vs. the USD and 5.3% vs. the EUR
- It now looks an obvious call that Ukraine will receive the 2nd tranche, however argue that cutting budget expenses is harmful to the ailing Ukrainian economy

## Authorities agree on IMF conditions

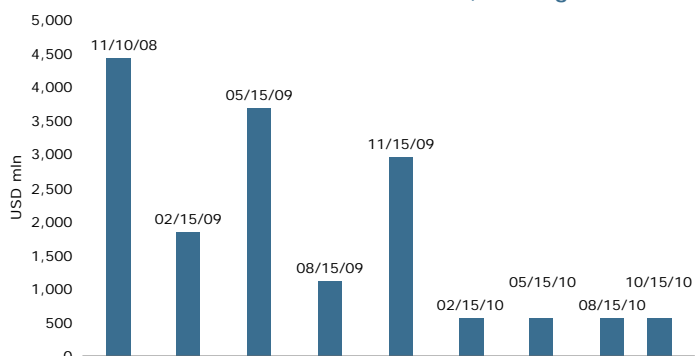
Yesterday, President Viktor Yushchenko, Prime Minister Yulia Tymoshenko, Verkhovna Rada Speaker Volodymyr Lytvyn, and National Bank Head Volodymyr Stelmakh agreed to comply with requirements set by the IMF to receive the second tranche (USD 1.8 bln) of the SDR 11 bln (USD 16.2 bln) stabilization loan.

The Ukrainian authorities agreed to:

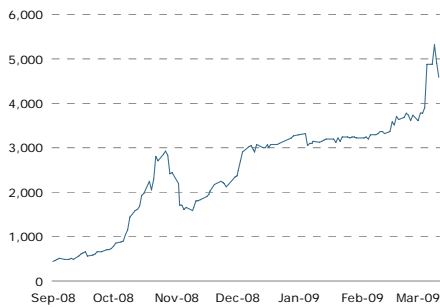
- Amend the 2009 budget for more realistic assumptions: it currently has GDP growth at 0.4% yoy, and external trade contracting just 7% yoy. The IMF has said the current budget could run a UAH 50 bln deficit (UAH 62 bln by our estimates). Media reports indicate both sides agreed to a UAH 30 bln deficit; exact budget changes have yet to be determined.
- Cancel budget provisions obliging the NBU to buy government bonds in unlimited amounts, and obtain Cabinet of Ministers' assent before refinancing commercial banks
- Abolish the requirement that a bank had to be under temporary administration to be recapitalized by the state

Yushchenko said today that he expects the IMF mission to return to Ukraine after March 16. Max Alier, the IMF's resident representative in Ukraine, said yesterday that Ukraine will receive the second tranche, though the timing is not clear.

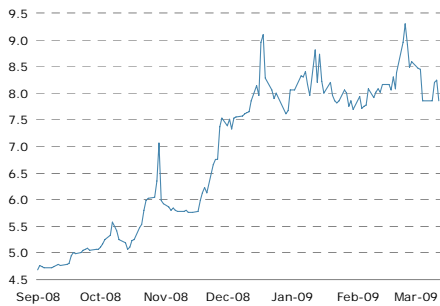
## Schedule of IMF loan tranches under Nov. 6, 2008 agreement



Note: Loan amounts are converted at the USD/SDR rate as of March 12 (0.679)  
Source: IMF

**Ukraine's 5Y CDS, bps**


Source: Bloomberg

**UAH/USD exchange rate**


Source: Bloomberg

**Market reaction**

CDS quotes on Ukraine's five-year sovereign debt dropped to 4,596 bps today from a historical high of 5,305 bps on March 10. The hryvnya appreciated 4.9% dod vs. the US dollar (UAH/USD 7.85) and 5.3% dod vs. the Euro (UAH/EUR 10.01), as of 16:30 today. We believe uncertainty about the second IMF tranche had been one of the key factors weighing against the UAH. Though it seems that this downside pressure has alleviated, we do not expect the hryvnya's strengthening to be long-lasting.

**Our view**

It looks like an obvious call that Ukraine will receive the second tranche. We believe that the abolishment of the NBU's obligation to buy government bonds and obtain Cabinet permission before refinancing commercial banks will markedly decrease the probability of runaway inflation in 2009. The relaxation of commercial bank recapitalization requirements will widen the range of banks willing to receive state capital injections.

As we expected, the IMF is flexible with Ukraine on its budget deficit in 2009. However, we contend that curtailing budget expenditures is highly undesirable. In fact, expenses have already eroded in real terms: while consumer prices surged 22.3% yoy over 2008, budget expenses for 2009 were only raised 4.9% yoy.

Decreasing budget expenses while the economy is already suffering from a drastic reduction in aggregate demand would only eat into demand further, compounding the problem. We argue that it is preferable to seek additional debt from international organizations or sovereigns than to cut budget expenses.

There have been signs that the government is exploring this route. Yesterday Russia confirmed that Ukraine approached it about a USD 5 bln loan. Last week, Tymoshenko said France and other European countries were ready to help Ukraine cover its budget deficit following agreement with the IMF on the second tranche of the loan.

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