



MEMU Supplement No.1-2008

Budget 2008: A temporary solution was found

The process for the Budget 2008 was heavily determined by the political process in the country. The pre-term Parliament elections were held at the end of September, and the new Government was formed only in December. While the first two drafts of the Budget 2008 were prepared by the previous Government, the new Cabinet of Ministers submitted a revised draft. It was submitted to the Verkhovna Rada only on December 26. During only one day, December 28, the Parliament approved the Budget 2008, thus breaking the procedures defined in the Budget Code. The approved Law was a compromise between all factions, though only the Parliament Coalition with the support of several deputies from the Communist Party voted for accepting the document.

For 2008 the central fiscal revenues and expenditures are planned at UAH 215.4 bn (24.2% of GDP) and UAH 232.4 bn (26.1% of GDP), respectively. The central fiscal deficit is envisaged at 2.1% of GDP and is to be financed by borrowings (UAH 10.0 bn) and privatisation receipts (UAH 8.9 bn). The list of objects for privatisation has not been published yet. Most likely the government will attempt to sell such large companies as the JSC Ukrtelecom and the chemical enterprise Odessa By-Port Plant. Also, the results of several privatisation deals conducted by the old government could be reconsidered. The government expects over-execution of the privatisation receipts by UAH 12 bn, which are to be spent for repaying devalued savings in the Oshchadbank. If so, the expected central fiscal deficit could *de-facto* reach 3.4% of GDP.

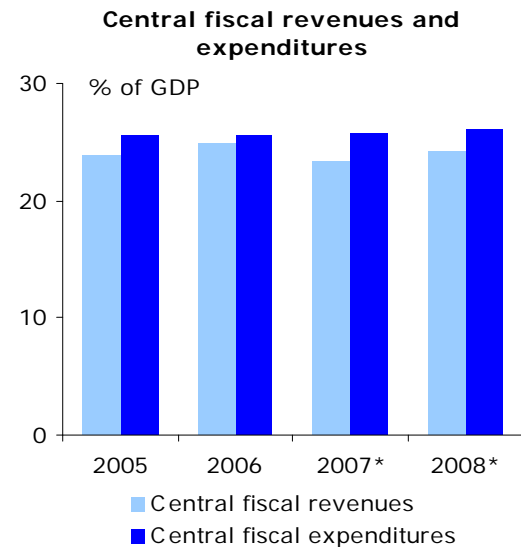
The fiscal parameters for 2008 are based on the numerous amendments to around a hundred of legislative acts approved as a separate chapter of the Budget 2008. These amendments are to be effective only for 2008. At the same time, the Government is required to submit to Parliament respective laws on amendments separately, in order to update the legislation for following years. The amendments concern legislation on taxation, social security, provision of social privileges, etc.

One of the hotly debated budget articles concerned the VAT regime for the agricultural producers. As a result of negotiations, the zero VAT rate for these producers will be abolished only in the year following Ukraine's WTO accession. The postponement of the VAT introduction for such enterprises deprives the state of an additional revenue source and does not allow equating tax burden among economic agents.

The new Cabinet of Ministers did not revise already high social standards foreseen in the Draft State Budget Law prepared by the previous Government. Also, the suggested increase in childbirth grants with the differentiation of their size depending on the number of children in the family remained unchanged. At the same time, the government introduced targeting while providing social assistance. In particular, after May 1, 2008, many types of privileges are to be provided only to eligible individuals if their incomes are lower than social privilege. As it was promised during elections, most of privileges to people deputies were abolished. Besides, a maximum size of pension benefits was defined.

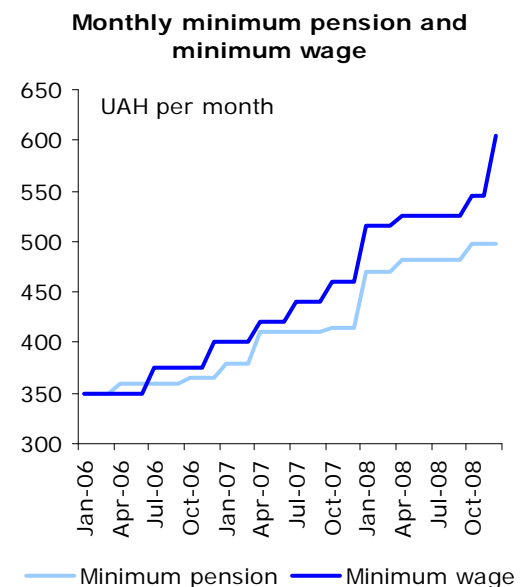
The compensation of devalued savings in Oshchadbank – one of the key social promises of Yulia Tymoshenko Bloc's election campaign – has been only partially addressed in the Budget 2008. It is planned to direct UAH 6.0 bn for cash compensations. In addition to the economically questionable repayment of savings from an expected over-execution of privatisation receipts, the government plans to introduce the procedure, according to which individuals would be able to use the devalued savings in Oshchadbank for utility payments and for the purchase of domestically produced goods. While the first type of payments might worsen payment transparency, the implementation of the second remains very unclear.

As shown, the adopted Budget 2008 retained its high social bias, while the execution of the privatisation plan remains very challenging and uncertain. According to the adopted Budget Law, the amendments to the State Budget-2008 are to be submitted by March 1, 2008. Thus, the current Budget is by definition of a temporary nature.



* Government plan

Source: the State Treasury reports, the State Budget Law for 2007 with amendments, the State Budget Law for 2008.



Source: State Budget Laws for 2006, 2007 and 2008

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Quarterly trends

National accounts		Q3 04	Q4 04	Q1 05	Q2 05	Q3 05	Q4 05	Q1 06	Q2 06	Q3 06	Q4 06	Q1 07	Q2 07	Q3 07
GDP	UAH bn	99.4	100.1	84.3	97.5	119.4	123.6	105.4	124.1	150.4	157.7	133.1	161.4	195.6
GDP (real)	% yoy	14.3	9.1	4.9	3.4	1.4	1.7	4.1	6.8	6.9	9.5	8.0	7.9	6.4
Households consumption (real)	% yoy	9.7	12.5	14.3	17.7	17.0	17.1	20.2	18.2	11.8	9.9	14.7	15.5	15.2
State consumption (real)	% yoy	3.9	0.9	6.1	0.0	1.0	4.0	9.6	5.8	5.8	1.0	0.8	6.2	4.4
Gross fixed capital formation (real)	% yoy	23.8	16.8	-2.3	-0.5	0.2	0.3	19.9	19.3	17.9	18.3	24.4	23.5	18.9
Exports of goods and services (real)	% yoy	14.3	11.7	-0.6	-14.0	-12.7	-15.5	-14.9	-9.6	3.2	1.0	4.9	5.2	0.1
Imports of goods and services (real)	% yoy	7.2	8.7	2.8	3.2	3.9	-0.9	10.7	0.9	8.3	6.4	12.9	19.6	13.7
Agriculture, hunting, forestry (real)*	% yoy	35.6	11.3	5.8	8.3	2.6	-7.2	3.8	2.8	-5.6	8.1	4.8	6.8	-9.3
Manufacturing industry (real)*	% yoy	9.9	6.9	7.0	1.8	-1.1	2.0	-1.5	6.1	7.3	7.2	15.0	13.2	13.1
Construction (real)*	% yoy	11.9	23.3	-8.4	-11.3	-8.5	-7.5	0.1	0.8	1.4	4.2	13.3	8.2	12.7
Trade, repair services (real)*	% yoy	13.9	2.5	-2.1	-10.7	-11.7	-11.9	6.2	16.4	20.0	21.9	14.3	17.5	25.3
Transport (real)*	% yoy	12.5	6.4	6.6	5.7	2.8	7.8	4.9	7.7	9.4	5.3	7.0	5.6	8
Balance of payments														
Current account balance	USD bn	2.1	1.1	1.6	0.6	0.4	-0.1	-0.8	0.0	0.5	-1.4	-1.3	-0.7	-0.2
Current account balance	% of GDP	11.0	5.7	10.1	3.2	1.7	-0.4	-3.7	0.0	1.7	-4.3	-5.0	-2.0	-2.2
Trade balance in goods	USD m	774	482	1020	-236	-1131	-788	-1353	-935	-884	-2022	-1753	-1430	-2195
Trade balance in services	USD m	749	157	188	392	1035	191	219	506	1054	347	50	403	1548
Current transfers	USD m	720	623	626	694	745	780	622	790	851	910	789	923	1054
Direct investment (FDI)	USD m	420	344	247	365	477	6474	1053	1389	1636	1258	1162	1772	3756
Portfolio investments	USD m	1313	156	397	923	90	1347	4	-141	370	3350	1818	1519	517
Gross international reserves	USD bn	12.1	9.5	12.0	13.1	14.3	19.4	17.3	17.6	19.1	22.3	23.5	25.6	30.6
Exchange rate, UAH/USD	aop	5.31	5.31	5.30	5.10	5.05	5.05	5.05	5.05	5.05	5.05	5.05	5.05	5.1
Fiscal indicators														
Consolidated fiscal revenues	% of GDP	26.3	25.9	32.1	35.1	31.5	31.0	31.2	31.7	31.9	32.8	33.3	32.8	30.8
Personal income tax	% of GDP	3.8	3.8	4.3	4.4	3.9	4.2	4.4	4.6	4.1	4.1	5.1	5.3	4.9
Enterprise profits tax	% of GDP	4.1	6.1	4.8	5.9	5.3	6.3	3.4	4.6	4.3	6.7	3.8	4.1	4.1
Value-added tax	% of GDP	5.1	4.1	8.6	9.2	7.9	7.3	9.2	9.2	9.7	9.3	10.4	9.8	8.7
Excise tax	% of GDP	2.0	1.8	2.0	2.0	2.0	1.7	1.8	1.7	1.5	1.5	1.8	1.7	1.6
Consolidated fiscal expenditures	% of GDP	26.8	35.2	28.3	36.4	28.1	41.7	30.9	32.8	29.4	36.6	28.4	31.0	29.6
Current expenditures	% of GDP	21.7	27.2	26.5	33.6	24.0	34.2	28.9	29.7	24.9	29.2	26.9	28.4	25.9
Capital expenditures	% of GDP	5.1	8.0	1.8	2.7	4.1	7.5	1.9	3.2	4.5	7.4	1.6	2.6	3.7
Consolidated fiscal balance	% of GDP	-0.5	-9.3	3.7	1.0	-5.0	6.2	-0.4	1.1	-2.4	4.0	-4.8	1.7	1.2
Privatisation receipts	% of GDP	3.5	1.0	0.2	0.6	0.6	16.0	0.1	0.1	0.1	0.1	0.5	0.5	0.3
Labour market														
Average wage (real)	% yoy	14.7	15.4	15.0	19.0	19.6	26.4	23.8	22.6	18.8	11.3	14.7	13.9	14.9
Household income (real)	% yoy	11.3	16.6	24.0	28.0	19.4	18.9	22.1	18.6	20.3	16.3	17.5	17.4	14.9
Unemployment rate (ILO methodology)	% cum	8.1	8.7	8.7	7.1	5.2	7.8	7.9	6.8	6.4	6.8	7.4	6.6	6.2
Banking system														
Monetary aggregate M0	% yoy cum	37.1	27.9	28.2	39.1	31.1	42.2	36.2	25.3	23.7	24.5	22.9	30.4	36.4
Monetary aggregate M2	% yoy cum	51.5	32.3	38.9	37.4	31.3	53.9	39.2	36.6	36.7	34.3	38.6	40.7	47.8
Household deposits in national currency	% yoy cum	67.9	26.2	28.3	31.6	30.4	90.8	54.6	41.1	39.7	37.3	50.7	56.3	64.8
Household deposits in foreign currency	% yoy cum	55.2	54.3	51.8	45.4	46.4	59.1	54.5	66.2	64.3	57.5	52.3	43.8	38.4
Com. bank credits in national currency	% yoy cum	44.3	29.4	28.3	32.6	43.4	58.7	59.8	53.7	49.0	52.3	52.4	57.2	60.7
Com. bank credits in foreign currency	% yoy cum	43.5	32.2	33.1	36.8	47.1	66.3	72.0	82.1	90.4	95.4	98.9	97.4	91.0
Long-term com. bank credits	% yoy cum	82.7	57.1	49.5	53.0	70.1	84.6	87.6	86.7	76.6	79.5	84.1	86.5	87.9
Long-term com. bank credits	% of total	50.9	54.2	54.4	56.1	59.7	61.8	63.1	63.4	63.5	64.9	65.8	67.3	68.2
Average lending rate on national cur. credits	% p.a.	17.0	17.6	17.0	15.4	15.4	16.4	15.8	15.5	14.6	15.1	14.0	13.9	13.7
Average lending rate on foreign cur. credits	% p.a.	12.6	12.2	12.1	11.0	11.3	11.7	11.5	11.3	11.3	11.5	11.5	11.4	11.3

SOURCES: National Bank of Ukraine, State Committee of Statistics, State Treasury, Ministry of Finance, IER estimates

* change in value added

° preliminary

Notes:
yoy year on year change

p.a. per annum