- **Russia.** In December, Russia agreed to reduce the price of natural gas for Ukraine by approximately 30% in the first quarter of 2014. Russia also promised to purchase Ukrainian Eurobonds at USD 15 bn with the yield at 5% p.a. These steps were a part of the agreement reached after a series of negotiations between Ukrainian President Viktor Yanukovych and his Russian counterpart Vladimir Putin. It is still not officially known whether Ukraine made any obligations in return for Russia's concessions. The financial aid is seen as a compensation for the decision of Ukraine to refuse to sign the Association Agreement (AA) with the European Union. That decision seemingly improved tense relations between Ukraine and Russia. Earlier in 2013, Russia banned imports of some goods from Ukraine, threatened to extend the ban on a number of products, and demanded Ukraine to pay USD 7 bn penalty for an alleged violation of a "take or pay" provision of gas import contract. Russia's pressure was intended to prevent Ukraine from signing the AA and ensure a full membership of the country in the Customs Union of Belarus, Kazakhstan, and Russia (CU). However, Ukraine has not yet made any public commitment regarding its membership in the CU. It is expected that Russia will continue to provide aid to Ukraine in 2014 if Ukrainian authorities coordinate policy-making with Russia, at least in the area of foreign affairs. Therefore, Ukraine is not likely to sign the AA with the EU at least until the next Presidential election in 2015. The accession to the CU is also unlikely because of strong opposition to this idea in Ukraine.
- **Political crisis.** The political crises that began in November after Ukraine refused to sign the Association Agreement (AA) with the EU persisted in December. Mass demonstrations continued to take place across the country. Their scale decreased at the end of the month, but remained large as hundreds of thousand people participate in rallies at each weekend. Protesters also continued to occupy Maidan Nezalezhnosti, the central square of Kyiv, and a part of Kyiv City Hall. Protesters demanded resignation of the Government and the President of Ukraine, and opposed to the accession of Ukraine to the Customs Union of Belarus, Kazakhstan, and Russia (CU). The situation looks like a stalemate because a large number of protesters are determined to continue manifestations until their demands are met but the authorities refuse to make any concessions. The authorities mostly avoid using heavy force to stop the civil unrest being afraid of sanctions from developed countrie and further escalation of protests. The protests may last long in 2014 maintaining a high level of political uncertainty. The confrontation may aggravate because the most active protesters are exposed to frequent criminal attacks.
- ***Real industrial output continued to decline.*** The trends in industry did not change substantially in November. In particular, industrial output declined by 4.7% yoy as domestic and external demand remained weak. Output in metallurgy dropped by 11.8% yoy. Machine building reduced production by 17.2% yoy. In particular, production of railway carriages and locomotives dropped by 45.7% yoy due to sharp drop in demand from Russia. At the same time, production of cars grew by 8.8% yoy likely due to increased trade protection. As Odessa oil refinery renewed its work in end September, output of oil refineries grew by 7.8% yoy. Good harvest contained costs in food production and led to increase in meat and milk processing as well as sunflower oil production. Nevertheless, sharp drop in sugar production by 29% yoy, and drop in confectionary production by 10% yoy led food production to drop by 7.8% yoy. Overall, in eleven months of 2013 agricultural production grew by 11.7% yoy due to record grain harvest and high harvest of other crops. Livestock production grew by 4.5% yoy. Between January and November retail trade growth decelerated to 9.2% yoy likely to slowdown in real disposable income growth. Lower coal production (largest component of rail freight) and lower rail transit (in part due to re-routing of cargoes to own ports by Russia) resulted in drop of freight turnover by 4.5% yoy. In

November drop in construction decelerated to 10.3% yoy due to statistical base effect. Residential construction as previously grew by 4.2% yoy but it accounts for less than 20% of construction work performed.

- **Energy sector: Ukraine receives cheaper gas.** On December 17, the Naftogas of Ukraine and Russian Gazprom signed an addendum to the gas agreement of 2009. According to new arrangements the coefficient k in the gas price formula is set in a way that the price of gas in the first quarter of 2014 equals USD 268.5 per thousand cubic meters. However, the "take or pay" clause of the contract is left untouched while the k coefficient needs to be defined every quarter in additional agreements between the Naftogas and the Gazprom. Therefore, the predictability of the future gas price is under concern. Besides, there could also be other impacts. In particular, lower price of gas may make recently started projects on alternative gas sources unprofitable. As a result, diversification of energy resources would not be reached. Moreover, cheaper gas also discourages Ukrainian enterprises from investing into energy efficiency projects that might have increased the companies' competitiveness.
- **Privatisation: Continued privatization of the energy sector.** On December 24th, the State Property Fund of Ukraine (SPFU) sold a 75% stake in Volynoblenerho, a power distribution company, for UAH 462 m. The selling price was marginally higher than the initial bid (UAH 457 m). The buyer was Ukreastgas LLC, which bought the Kharkiv combined heat and power generating plant No.5 in 2012. The SPFU has not disclosed yet whether the money were transferred to the State Budget till the end of the year. According to the draft State Budget for 2014 the planned privatization receipts are expected at UAH 17 bn. It is unclear which companies are to be sold to ensure such high receipts. One of the companies, which is likely to be on sale, is Odesa by-port plant.

Ukraine: Economic Indicators 2011 - 2014

		2010	2011	2012	Q1 13	Q2 13	Q3 13	Oct	Nov	Dec
GDP (real)	% yoy	4.1	5.2	0.2	-1.1	-1.3	-1.3			
Industrial production (real)	% yoy cum.	11.2	7.3	-1.8	-5.0	-5.3	-5.2	-5.2	-5.0	
Agricultural prod. (real)	% yoy cum.	-1.0	17.5	-4.5	5.8	15.4	3.0	9.9	11.7	
CPI	% yoy eop	9.1	4.6	-0.2	-0.8	-0.1	-0.5	-0.1	0.2	0.5
Current account	% GDP. cum.	-1.7	-5.6	-9.0	-7.2	-4.5	-10.7			
Fiscal balance	% GDP	-6.0	-1.8	-3.6	-1.9	-6.4	3.6			
External state debt (total)	% GDP eop	25.6	22.8	22.0						
Gross international reserves	USD bn cum.	36.7	31.8	31.4	24.7	23.2	21.6	20.6	18.8	20.4
Exchange rate (official)	EUR aop	10.53	11.09	10.27	10.55	10.44	10.58	10.90	10.79	10.94

Source: IER.

For further information: Institute for Economic Research and Policy Consulting (link: http://www.ier.com.ua).