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BUDGET AND ECONOMY OF UKRAINE

KEY TRENDS OF JANUARY-MARCH 2011



**INSTITUTE FOR BUDGETARY
AND SOCIO-ECONOMIC RESEARCH**

The monitoring materials have been prepared based on data of the State Treasury of Ukraine, State Statistics Committee of Ukraine, and other official sources. This booklet contains a brief review of Ukraine's budget and economy in January through March 2011, describing the key trends in the execution of the consolidated, State, and local budgets, and highlighting the main changes in the macroeconomic situation, and trends in the banking system, and their interrelation with budget indicators. A more in-depth analysis of the Ukrainian budget and economy in this period can be found in the IBSER publication *Budget Monitoring: Analysis of Budget Execution in January-March 2011*.

Budget and Economy. Key Trends of January-March 2011

This publication has been prepared by the following IBSER experts:

I.F.Shcherbyna, Director General
V.V.Zubenko, Deputy Director General, Director of PPB and Training Programs
A.Yu.Rudyk, Director, Department of Tax Policy and Monitoring
I.V.Samchynska, Director, Department of Financial Policy
A.I.Korniyenko, Deputy Director, Department of PPB and Trainings Programs
I.M.Pereli, Chief Economist/Financial Officer, Department of Financial Policy
M.S.Svyeshnikova, Banking Consultant

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Institute for Budgetary and Socio-Economic Research
15V, Borysohlibska St., 2nd Floor
Kyiv, 04070, Ukraine
Tel.: (044) 353-58-68, 492-97-80/81
Fax: (044) 492-97-83

BUDGET AND ECONOMY. KEY TRENDS OF JANUARY-MARCH 2011

Indicator	As of 1 April 2010	As of 1 April 2011
Consumer Price Index (vs. December of previous year), %	104.7	103.3
Gross bank assets, Hr bn	998.8	1 149.4
Amount of credits, Hr bn	696.7	742.6
including credits <i>to legal entities</i> , Hr bn	472.7	540.9
<i>credits to individuals</i> , Hr bn	224.0	201.7
Amount of deposits, Hr bn	338.0	439.6
including deposits <i>of legal entities</i> , Hr bn	118.3	152.0
<i>deposits of individuals</i> , Hr bn	219.7	287.6
State budget revenues, Hr bn	51.7	66.4
including transfers from local budgets into State budget, Hr bn	1.6	0.6
State budget expenditures, Hr bn	57.4	66.7
Crediting, balance, Hr bn	-0.2	0.6
State budget deficit (-)/ surplus (+), Hr bn	-5.5	0.9
Local budget revenues, Hr bn	32.2	38.8
including transfers from State budget to local budgets, Hr bn	15.1	20.1
Local budget expenditures, Hr bn	31.1	38.6

ANALYSIS OF MACROECONOMIC INDICATORS

The macroeconomic situation in January-March 2011 was characterized by a gradual resumption of economic growth. It occurred against a backdrop of minor inflation as well as a noticeable increase in the national currency exchange rate against the euro.

One of the reasons behind this economic recovery is a resumption of economic activity in many areas of the economy and a continued trend of increasing industrial output, even though at a slower pace than last year. Industrial production rose by 9.7%, year-on-year, in January-March 2011, against 11.2% for both the respective period of last year and the last year in general. Specifically, the production of machinery increased by 26.8%, that of chemical and petrochemical industry – by 18.0%, metals and finished metal products – by 11.7%, in particular, pipes by 50.8%, and agricultural produce – by 5.3%.

The change in real wages generally retains 2010's trend. Thus, after 10.2% growth in real wages in 2010 in general, they retraced in January 2011 (-13.2%), but then increased again in February and March (0.9% and 6.6, respectively). For comparison, these figures were (-13.3%), 0.1%, and 6.8%, respectively, in 2010. This change, however, was observed against a 9.2% overall decline in real wages in 2009. Compared to the same period of last year, real wages increased by 11.1% in Q1 2011 (by 5.1% in 2010). Also, retail trade turnover increased by 13.5%, which is a confirmation of the gradual recovery of domestic consumer demand.

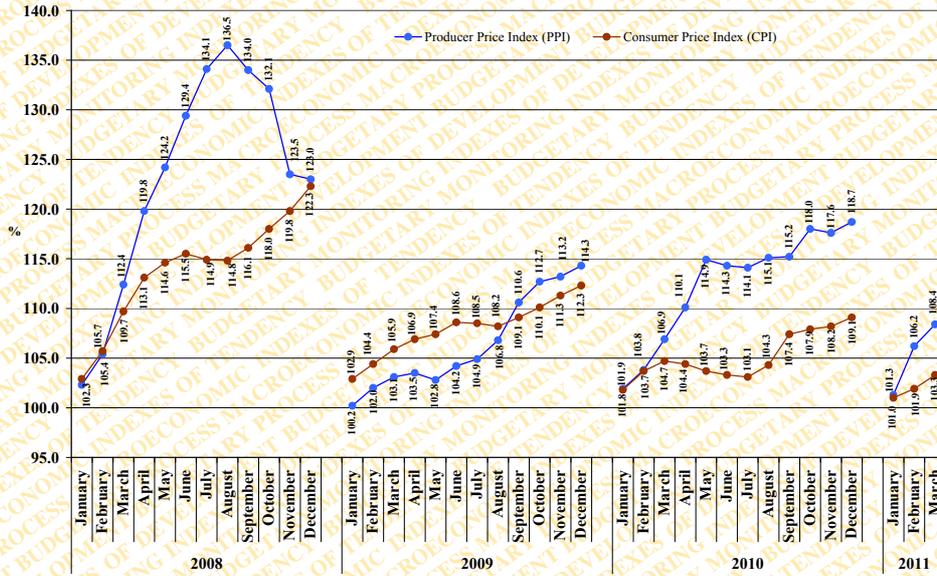
The Consumer Price Index (CPI) totaled 103.3% in Q1 2011 vs. 104.7% in 2010 (see Chart 1). The CPI growth is mainly explained by the price of vegetables increasing by 22.7%, fuel and lubricants by 20.2%, and hot water and heating services by 15.5%. At the same time, the prices of photographic and data processing equipment decreased by 1.1% in the reviewed period, those of audio equipment and household appliances fell by 0.4%, and telephone and fax service prices dropped by 0.1%. This reduction in prices occurred due to a decline in domestic demand for these types of goods against a backdrop of individuals' spending the greatest part of their income on food. At the same time, the prices of milk, cheese, and eggs decreased by 3.7%, those of clothing and footwear dropped by 0.3%. Therefore, households are now inclined to spend money on essential goods and, taking into account experts' forecasts and the unpredictability of economic development closer to autumn, save some part of their cash.

The Producer Price Index (PPI) amounted to 108.4%, which is 1.5ppt more than in Q1 2010. The highest PPI growth figures against December of last year were noted in the extraction of minerals, except fuel and energy minerals (by 25.8%), oil refining (by 13.4%), production of metals and finished metal products (by 10.7%), and production of sugar (by 7.0%). On the whole, the extractive industry prices increased by 16.3%, the manufacturing industry prices by 6.4%, and prices in the production and distribution of electric power, gas, and water increased by 10.3%¹.

¹ www.ukrstat.gov.ua

Chart 1

Dynamics of Price Indices in 2008-2011

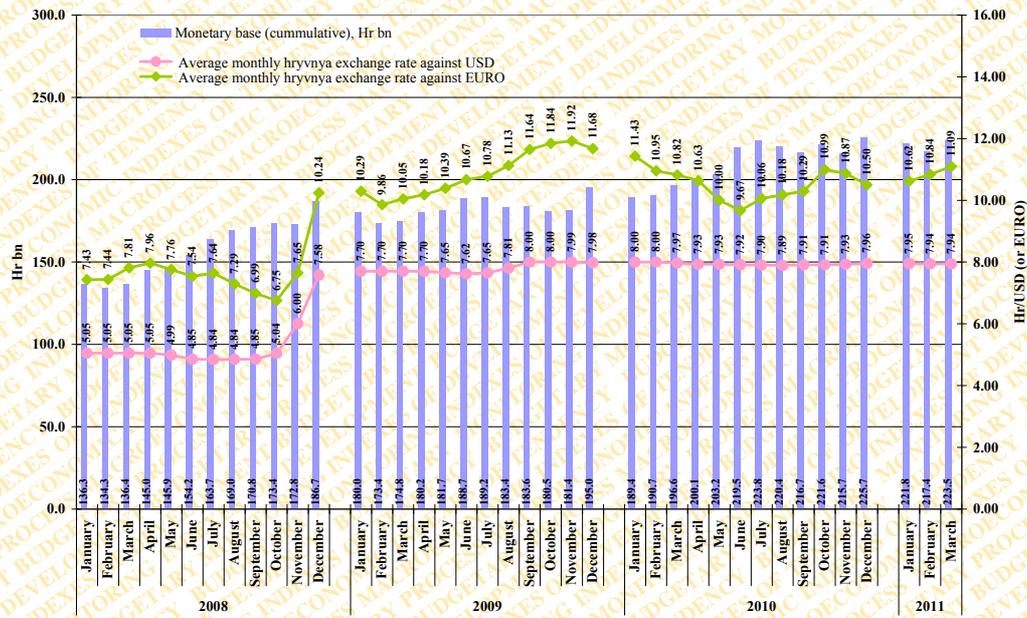


The monetary and credit market reflected the following trends in Q1 2011. Further growth of deposit accounts in banks continued, which has led to reducing the cost of money. Given the lower inflation level and growing business activity throughout the reviewed period, favorable conditions emerged for banks to resume their lending to the real sector in the economy, which, in turn, has affected an increase in the average weighted cost of credits in the national currency.

The average monthly hryvnya exchange rate against U.S. dollar was relatively stable throughout Q1 2011 (at Hr 7.94 - Hr 7.95 to \$1), and reflected the trend of a gradual reduction in the cost of the national currency against the euro² (see Chart 2). The average official exchange rate of the Ukrainian hryvnya against the euro was Hr 10.85 to 1 euro in the reviewed period.

Chart 2

Dynamics of the Ukrainian Hryvnya Exchange Rate against U.S. Dollar and Euro in 2008-2011



² www.bank.gov.ua/statist/Stat_data/Exchange_r.xls

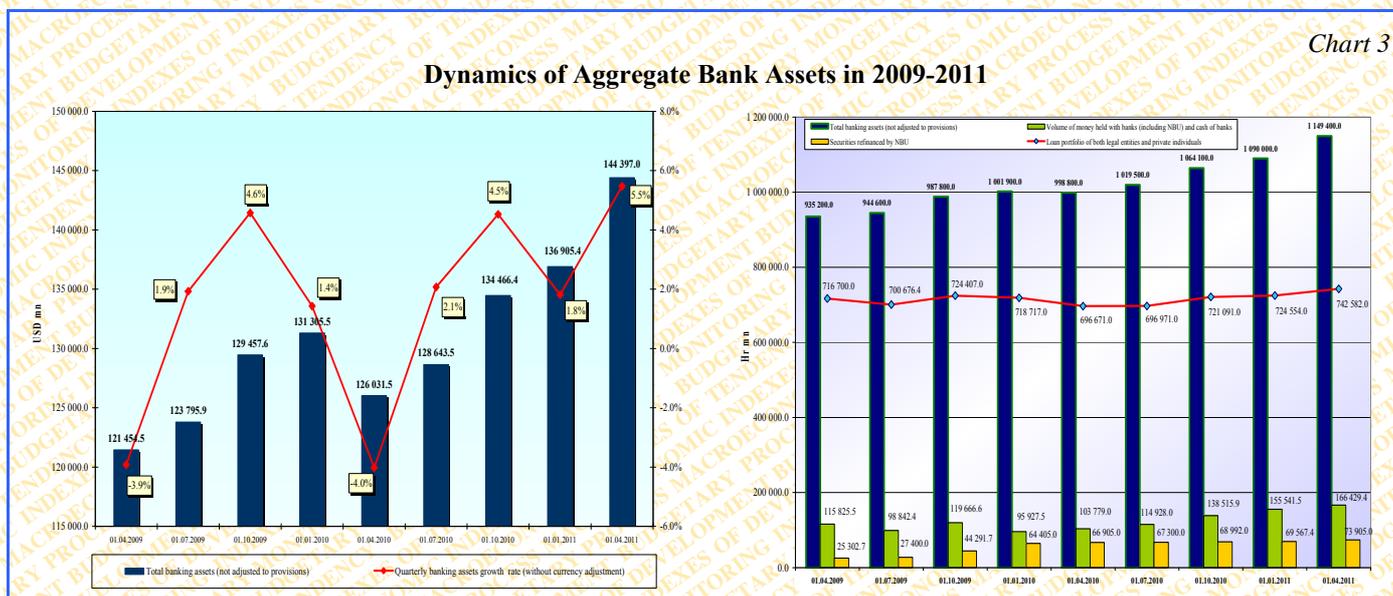
BANKING SYSTEM TRENDS

In the first quarter of 2011, the **Ukrainian banking system** was characterized by:

- the NBU pursuing a strict monetary and credit policy and taking steps to limit pressures on the currency exchange rate, and banks conducting a more flexible interest-rate policy;
- a sufficient level of banking system liquidity, lack of demand for refinancing transactions, and growth of cash outside of banks;
- 5.5% growth in the total assets of the banking system;
- a continued trend of minor growth in the loan portfolio of legal entities (+4.0% or +Hr 20.8bn);
- further growth of client deposits, with deposits of legal entities increasing by Hr 15.9bn or 6.7%, and those of individuals by Hr 14.2bn or 5.8%.
- a negative financial result of the banking system of Hr 210.8mn, which was mainly caused by the loss-bearing operations of the banks in temporary administration and the banks being liquidated, as well as a slower growth rate in the operational result due to suspended lending operations;
- a slight increase in the share of overdue debts in the total client credit debt from 11.24% at the end of 2010 to 11.52% as of 1 April 2011. In absolute terms, the amount of overdue debt increased insignificantly, by 0.9%, to Hr 85.58bn;
- growth of the share of foreign capital in the total authorized capital of the Ukrainian banking system by 0.9ppt to 41.5%. However, the total number of active banks with foreign capital decreased by one bank to 54 banks. The number of banks with 100 percent foreign capital remained unchanged at 20.

As of 1 April 2011, 176 banks had licenses for conducting the banking business from the National Bank of Ukraine. Eighteen banks were in the process of liquidation, including seventeen banks liquidated by NBU decision and one bank liquidated by decision of commercial (arbitration) courts. Five banks continue under temporary administration.

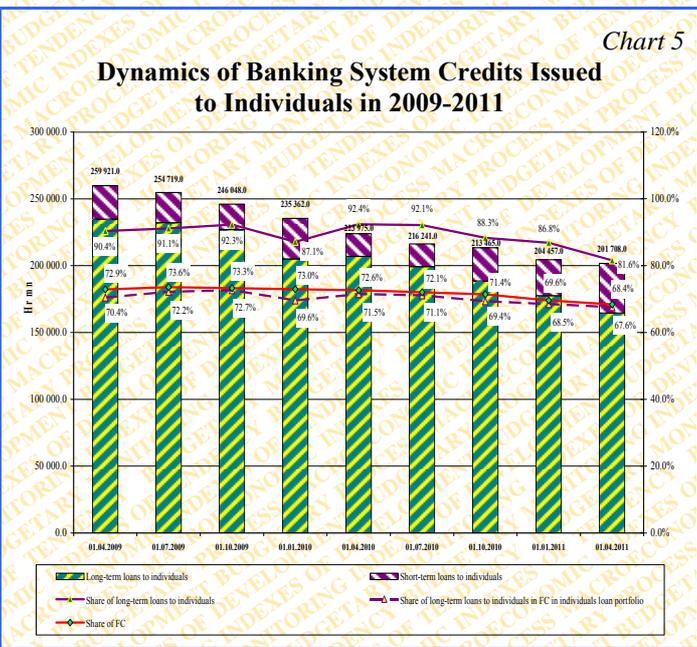
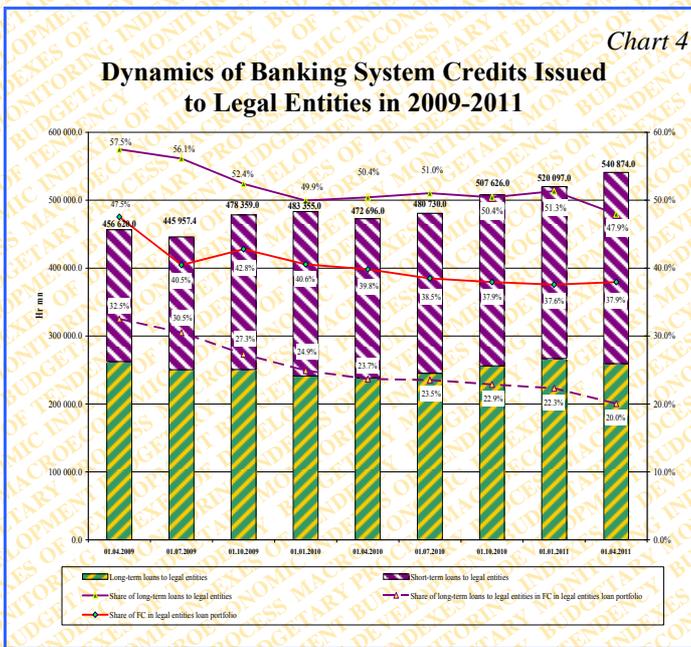
The total assets of the Ukrainian banking system increased slightly in Q1 2011. Thus, the aggregate assets of the Ukrainian banking system increased by +5.5% in Q1 2011 vs. Q4 2010 and reached Hr 1,149.4bn (see Chart 3).



The clients' loan portfolio increased by 2.5% and reached Hr 742.6bn, with the main contributor still being a positive dynamics of the loan portfolio of corporate clients.

Despite their still great significance, the share of foreign-currency credits continues to decline (46.2% at the end of Q1 2011 compared to 46.6% at the end of 2010). This is mainly due to a continued downward trend in the loan portfolio issued to retail clients in foreign currencies and more exacting requirements to the accumulation of debt reserves in foreign currencies. The key reasons behind banks' low lending activity still include a high level of problem debts, high interest rates, and the low creditworthiness of the majority of borrowers.

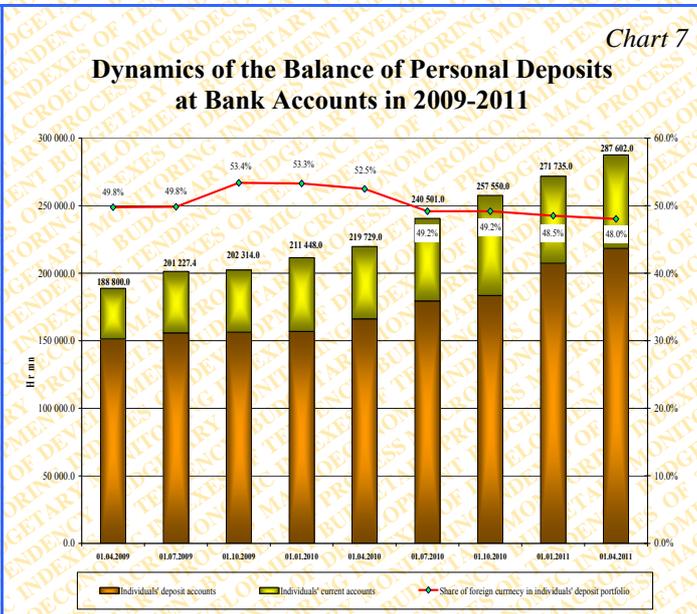
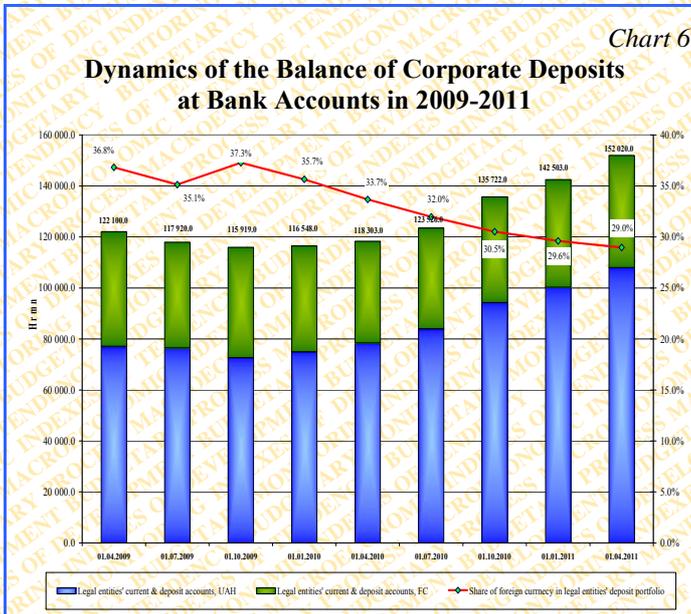
As of 1 April 2011, the loan portfolio of legal entities totaled Hr 540.9bn or 72.8% of the total client loan portfolio, and the individuals' loan portfolio totaled Hr 201.7bn or 27.2% of the total client loan portfolio (see Chart 4 and Chart 5).



Given the suspension of lending to clients in general, the rate of growth of credits issued to legal entities was a positive one at +4.0% (compared to +2.5% in Q4 2010).

The pace of repayment of the individuals' loan portfolio is still higher than the growth in new lending. It should be noted that the rate of reduction of the individuals' loan portfolio has slowed down and a positive growth in the loan portfolio of individuals in the national currency was recorded in Q1 2011. The pace of repayment of credits issued to individuals has slowed down to 1.3% compared to 4.2% in Q4 2010.

The deposit portfolio of economic agents totaled Hr 152.0bn or 17.7% of total liabilities, and the deposit portfolio of individuals totaled Hr 287.6bn or 33.6% (see Chart 6 and Chart 7).



Both corporate and personal deposits continued to trend upward.

The funds of legal entities increased by 6.7%. Also, the foreign-currency deposits of legal entities in dollar equivalent increased by \$0.24bn or 4.6%, while the national-currency deposits increased by Hr 8.0bn or 8.0%.

The funds of individuals increased by 5.8%. Personal deposits in the national currency increased by Hr 9.5bn or 6.8%, and those in foreign currencies by \$0.8bn in dollar equivalent or by 4.8%. The age structure of personal deposits at banks is as follows: time deposits total Hr 217.6bn or 75.9% of all personal deposits, and call deposits amount to Hr 69.0bn or 24.1%.

One characteristic phenomenon is an increasing proportion of personal deposits in the national currency in the total amount of personal deposits: from 51.5% in 2010 to 52.0% in Q1 2011, which testifies to a gradual restoration of the population's trust in the national currency in an environment of stable exchange rates against foreign currencies.

A significant proportion of the increase in personal time deposits in Q1 2011 was posted by PrivatBank (+Hr 5.3bn), Oshchadbank (+Hr 917mn), Ukreximbank (+Hr 864mn), and Delta Bank (+Hr 700mn).

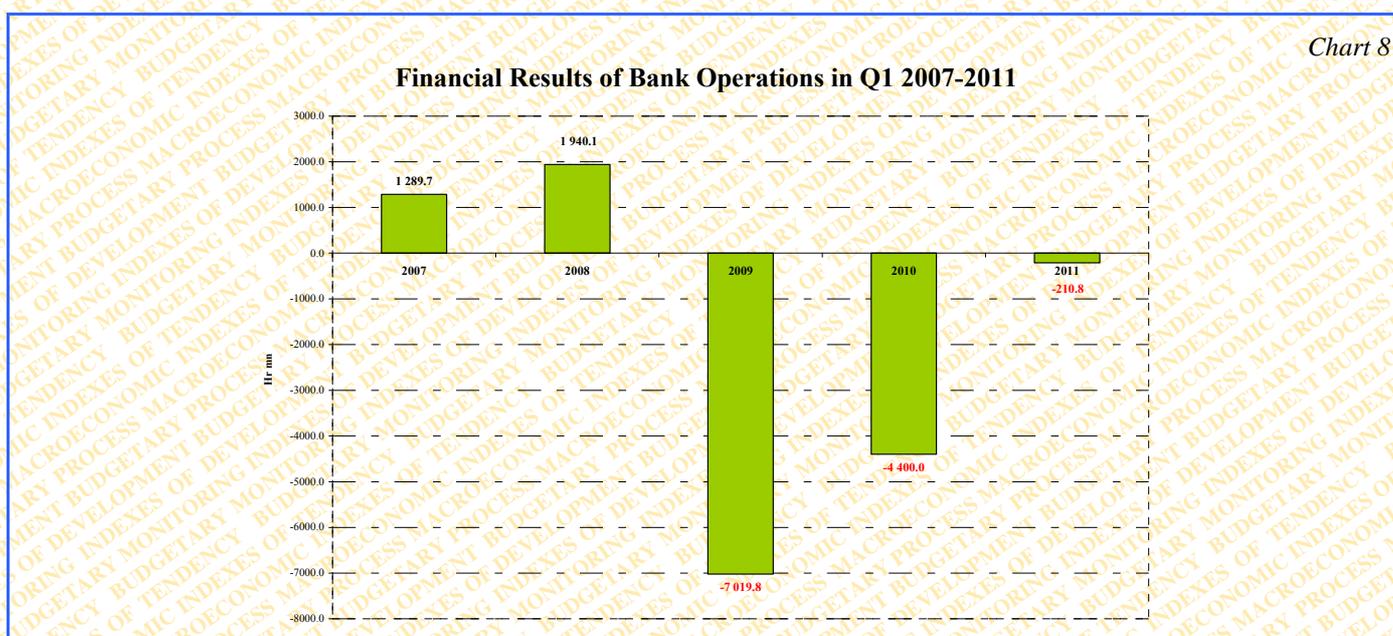
The banking system is experiencing no shortage of liquidity. The correspondent accounts of banks increased by 16.2% to Hr 19.4bn since the beginning of the year. Also, the banks had little demand for refinancing transactions: they totaled Hr 7.9mn year-to-date, and the repayment of previously issued refinancing credits totaled Hr 3.8bn (some part repaid ahead of schedule).

The amount of mandatory reserves accumulated by banks totaled Hr 12.7bn including Hr 7.3bn in funds remitted to the separate account. The high rates of growth of client deposits in Q1 2011 and of cash outside of banks both impacted the dynamics of the money supply, the amount of which increased by 4.1% year-to-date to Hr 622.3bn. The monetary base decreased by 1.0% to Hr 223.5bn.

The equity of banks increased by 3.0% and reached Hr 141.9bn or 14.2% of their liabilities. Their registered authorized capital increased by 0.8% to Hr 147.1bn.

The banks posted a loss of Hr 210.8mn in Q1 2011 (a loss of Hr 4.4bn was posted in the respective period of 2010) (see Chart 8). The income of banks increased by 5.5% year-on-year and totaled Hr 34.4bn. Banks costs decreased by 6.6% and amounted to Hr 34.6bn. It should be noted that the present loss is mainly linked to the losses of problem banks (the aggregate loss of the five banks continuing under temporary administration, totals Hr 1.1bn). Without the losses of these banks, the banking system profit is estimated to have been about Hr 900mn.

The banks' total income consists primarily of 81.9% interest income and 11.4% commission income. The main expenditure items of banks include interest costs of Hr 14.4bn or 41.6%, other operating and general administrative costs of Hr 12.3bn or 34.6%, and deductions into reserves of Hr 7.2bn or 20.9%.



Analysts note a growth in bank profits before the formation of reserves, which is mainly caused by the banks' increased volume of interest and commission income. Based on operational results, the bank profits before reserves totaled Hr 6.8bn.

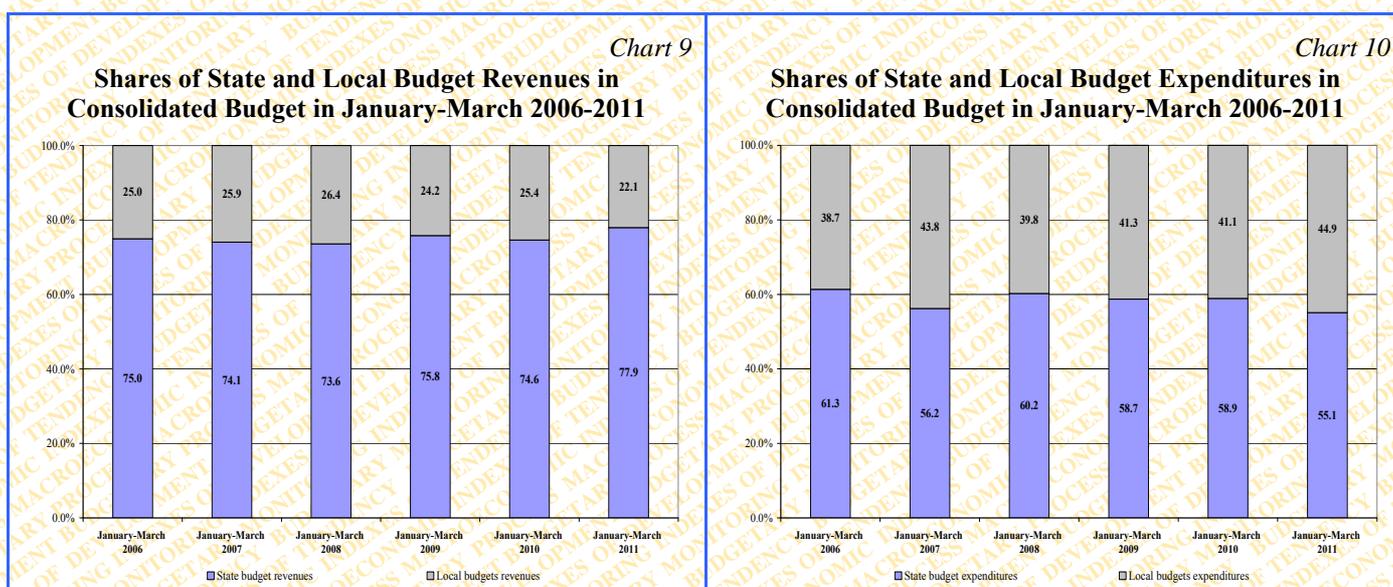
Thirty two (32) banks, or 20.3% of all banks in Ukraine, posted negative financial results. Rodovid Bank bears the largest share of the losses (-Hr 409mn).

The top ten most unprofitable banks also include banks with foreign capital, the most unprofitable of which are Forum Bank (-Hr 298mn), UkrSibbank (-Hr 170.6mn), and Prominvestbank (-Hr 49.0mn). The most profitable operations were PrivatBank (+Hr 435mn), OTP Bank (+Hr 269.5mn), and Citibank Ukraine (+Hr 125.4mn).

ACTUAL CONSOLIDATED BUDGET REVENUES AND EXPENDITURES

The actual intake of **consolidated budget revenues** totaled Hr 84.4bn in January-March 2011, which is 25.8% more year-on-year. This amounts to 23.1% of the annual plan (vs. 21.6% of the annual planning appropriations in Q1 2010). The share of local budget revenues in the consolidated budget structure decreased by 3.3ppt year-on-year to 22.1% in the period under review (see Chart 9).

Year-on-year, **consolidated budget expenditures** grew in the reviewed period up to Hr 84.5bn or by 17.8% (to compare: consolidated budget expenditures increased by 10.4% in 2010 year-on-year, and by 16.0% in 2009). The level of execution of consolidated budget expenditures amounted to 23.1% of the 2011 plan in the period under review (20.6% in Q1 2010). The structure of consolidated budget expenditures underwent some changes in January-March 2011 (see Chart 10). The share of local budget expenditures increased by 3.8ppt compared to the 2010 figure and amounted to 44.9%, which is the highest proportion of local budget expenditures in the overall consolidated budget structure since 2006. Social and cultural expenditures accounted for 67.1% of consolidated budget expenditures in Q1 2011 (66.0% in Q1 2010).



STATE BUDGET AND LOCAL BUDGET REVENUES

The actual revenues of the **State budget (without intergovernmental transfers)** totaled Hr 65.8bn, which is Hr 15.7bn or 31.3% more year-on-year. Budget revenues increased for nearly all items. For instance, the revenues from enterprise profit tax increased by Hr 2.2bn or by 23.5%, from value-added tax by Hr 8.1bn or 37.9%, excise tax by Hr 1.6bn or 30.0%, and taxes on international trade and external transactions increased by Hr 0.7bn or 46.2%. Also, the revenues from royalties and fees for fuel and energy resources more than doubled, totaling Hr 5.4bn.

A relatively high level of annual plan execution could be noted as one of the distinct features in Q1 2011 budget performance. As such, State budget revenue intake amounted to 23.6% in January-March 2011 compared to 18%-20% in the previous seven years. Notably, the annual plan for tax revenues was fulfilled by 24.4%, VAT by 27.1%, enterprise profit tax by 25.8% etc. This level of annual plan execution is indicative of the economy developing at a pace higher than expected this year, and, thus, there are grounds to increase the annual plan for State budget revenues already based on the Q1 performance.

Also, the amount of VAT refund from the budget more than doubled compared to last year and totaled Hr 8.9bn. At the same time, only Hr 0.7bn or 7.6% of the total refund due was reimbursed "automatically."

As a result of the above changes, the structure of State budget revenues shows some quite significant deviations compared to the same period in 2010. First, note should be made of an 11.0ppt growth in the share of tax revenues in the general structure of State budget revenues, which was caused by including the rent and fees for fuel and energy resources in the category of taxes. The same applies to a 9.7ppt increase in this category as other tax revenues, which now includes the rent and the above fees. (see Chart 11).

Chart 11

Structure of State Budget Revenues in January-March 2006-2011

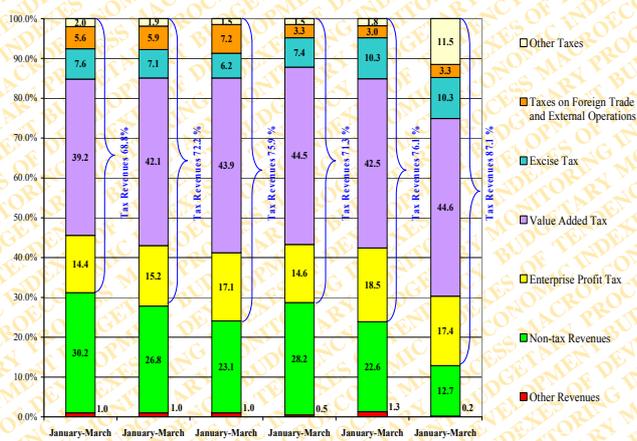
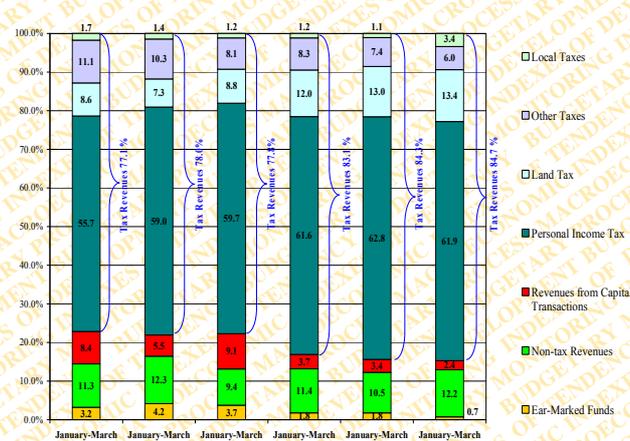


Chart 12

Structure of Local Budget Revenues in January-March 2006-2011



Local budget revenues (without intergovernmental transfers) totaled Hr 18.6bn, which is 11.8% (or Hr 9.5bn) more than in January-March 2010. Of the annual revenue intake plan approved by local councils, 22.3% was received. Of the year's revenue intake projected by the Ministry of Finance, 23.0% was received.

Tax revenues continued to grow as a share of local budget revenues, up to 84.7% (0.4ppt rise), along with an increase in the share of non-tax revenues (by 1.7ppt) (see Chart 12). Tax revenues (by 9.8%) and non-tax revenues (by 27.4%) increased in nominal terms year-on-year. At the same time, the revenues from capital transactions decreased by 23.7% and revenues of targeted funds fell by 54.7%.

The growth in tax revenue was significantly influenced by the dynamics of revenue from personal income tax, which increased by 7.8% against the 2010 figure and amounted to Hr 11.5bn. At the same time, the share of this tax decreased to 61.9% of all local budget revenues (without intergovernmental transfers).

Receipts from the payment for land grew throughout January-March (+12.6% against 2010). Also, their share in the structure of local budget revenues increased somewhat and amounts to 13.4%.

Local taxes and fees generated a total of Hr 634.0mn or 3.4 times more than last year, which increased their share in the structure of local budget revenues to 3.4% vs. 1.1%. This increase is explained by a change in the new version of the Budget Code of Ukraine and the Tax Code of Ukraine approved on 2 December 2010, local taxes and fees include a tax on property (to be introduced as of 1 January 2012), a fee for conducting certain types of business activity, parking fee, tourist charge, and single tax. The last tax generated Hr 469.0mn in revenues year-to-date, which is 10.5% more than in the same period of last year.

The new Tax Code also abolished the tax on owners of transport vehicles and other self-propelled machines and mechanisms, which has influenced the local budget revenues accordingly. At the same time, in January through March 2011, local budgets received a total of Hr 203.4mn from fees for the initial registration of vehicles and from the tax on owners of transport vehicles levied for the previous year, as part of the taxes on property.

STATE BUDGET AND LOCAL BUDGET EXPENDITURES

The actual expenditures of the State budget (with intergovernmental transfers) totaled Hr 66.7bn in Q1 2011, which amounts to 20.7% of the plan approved for 2011. Expenditures increased by Hr 9.3bn against Q1 2010 or by 16.2% (see Table 1), compared to Hr 6.4bn or 12.6% in Q1 2010 against the 2009 figure.

Table 1

**Comparison between Expenditures of the State Budget of Ukraine in Q1 2011 and Q1 2010
by Functional Classification of Expenditures and Crediting (KFKVK)**

KFKVK	Description as per Functional Classification of Expenditures and Crediting	Executed in Q1 2010, Hr mn	Executed in Q1 2011, Hr mn	Deviation (+/-) of Q1 2011 vs. Q1 2010	Structure (+/-) of Q1 2011 vs. Q1 2010	Growth in Q1 2011 vs. Q1 2010, %
1	EXPENDITURES TOTAL, including:	57 409.4	66 691.0	9 281.6	x	116.2
2	Expenditures subjected to significant cuts, total, including:	5 154.4	756.2	-4 398.3	x	14.7
0432	Gas and oil industry	2 602.2	–	-2 602.2	x	–
0160	Holding of elections and referendums	925.3	7.9	-917.4	x	0.9
0930	Vocational education	908.3	231.9	-676.4	x	25.5
0800	Spiritual and physical development	711.7	515.1	-196.6	x	72.4
0600	Housing and communal services	6.9	1.3	-5.7	x	18.1
3	Increase in expenditures, total	52 255.0	65 934.8	13 679.8	100.0	126.2
3.1	Intergovernmental transfers, debt servicing, and social protection of pensioners, total, including:	29 121.4	39 171.6	10 050.2	73.5	134.5
0180	Intergovernmental transfers	15 137.8	20 145.9	5 008.1	36.6	133.1
0170	Debt servicing	1 798.8	4 620.5	2 821.7	20.6	256.9
1020	Social protection of pensioners	12 184.7	14 405.2	2 220.5	16.2	118.2
3.2	Other priorities of increased expenditures, total, including:	15 979.2	18 539.8	2 560.5	18.7	116.0
0300	Public order, security, and judiciary	5 481.1	6 332.2	851.2	6.2	115.5
0940	Higher education	4 899.0	5 510.3	611.3	4.5	112.5
0456	Road building and maintenance	1 760.8	2 274.5	513.8	3.8	129.2
0200	Defense	2 345.0	2 623.4	278.4	2.0	111.9
0700	Healthcare	1 226.8	1 465.8	239.0	1.7	119.5
0500	Environmental protection	266.6	333.5	66.8	0.5	125.1
3.3	Other expenditures, total	7 154.3	8 223.5	1 069.1	7.8	114.9

As seen from Table 1 above, the State budget expenditures for the gas and oil industry have suffered the most significant cuts (-Hr 2.6bn). This is linked to the absence in the 2011 budget of the following expenditures: for compensation to NAK Naftohaz Ukrainy of the difference between the buying price of imported natural gas and its selling price for the provision of heat supply to the population (Hr 3.4bn in 2010); for holding elections (-Hr 1.0bn); expenditures for vocational education (-Hr 0.7bn) due to the transfer of the majority of vocational schools to financing by local governments. On the whole, expenditures were reduced by a total amount of nearly Hr 4.4bn.

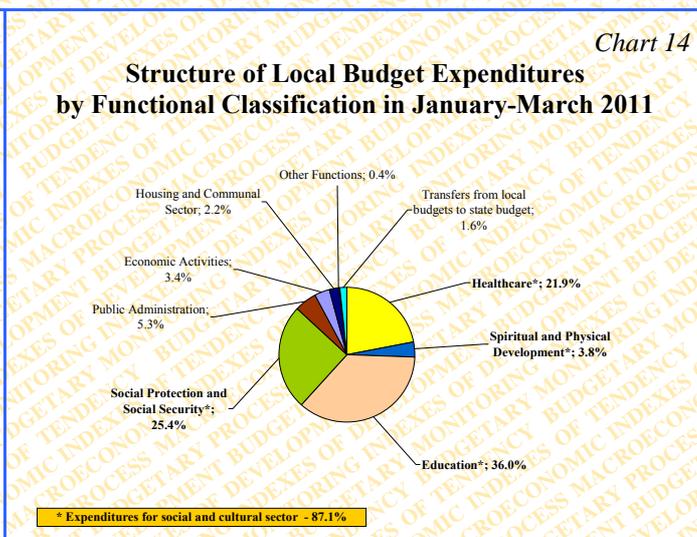
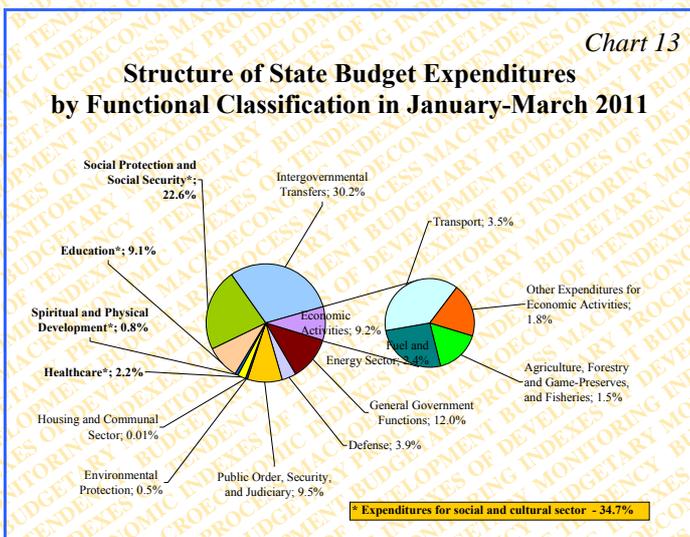
The remaining State budget expenditures increased by Hr 13.7bn in general. The main priorities of the public policy for increasing the State budget expenditures compared to last year (73.5% of the total amount) included intergovernmental transfers with 36.6% of the total increase in expenditures; debt servicing with 20.6%, and the social protection of pensioners with 16.2% of the increase.

Even though the share of social expenditures dropped to 34.7% (see Chart 13) or by 4.7ppt, their amount increased by Hr 5.2bn or by 29.0%. At the same time, expenditures for the social protection of pensioners nearly doubled, and presently accounts for 21.6% of expenditures. *To compare, the proportions of expenditures for the social protection of pensioners in some Member States of the European Union: 2.4% in Lithuania, 7.6% in Hungary, 9.7% in Slovenia, and 11.0% in France. It amounted to 19.8% in Ukraine at that time.* This is another argument in favor of implementing pension reform in Ukraine and reducing the burden of pension allowances on the budget.

Local budget expenditures totaled Hr 38.6bn, which is 24.2% more year-on-year. This equals 23.2% of the annual estimate of the Ministry of Finance and 22.6% of the plan approved by local councils.

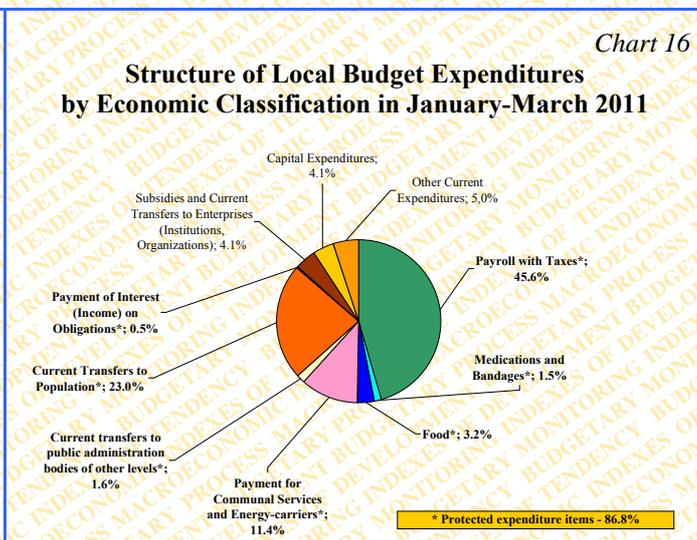
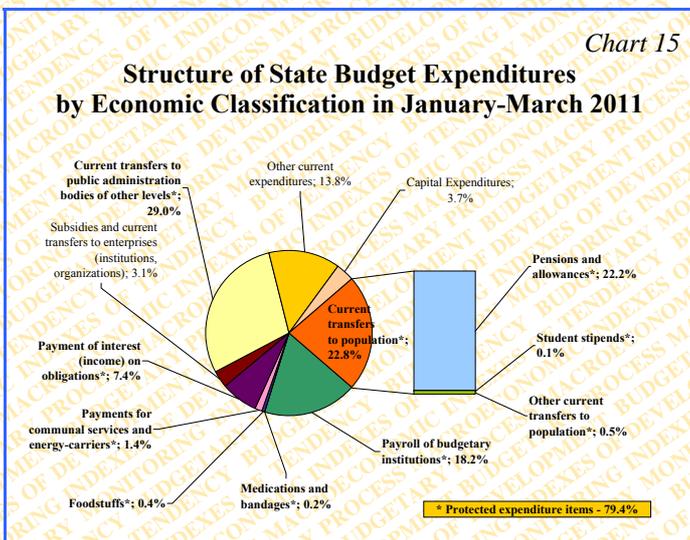
The share of local budget expenditures used for society and culture amounted to 87.1% in the reporting period (see Chart 14), which is 1.5ppt more year-on-year.

Based on functional classification, the greatest changes occurred in expenditures for economic activity, whose share increased by 2.0ppt and amounts to 3.4%, and expenditures for social protection and social security, which grew by 1.9ppt to 25.4%. At the same time, there was a minor increase in the share of expenditures for education (by 1.3ppt to 36.0%) and a decrease in health expenditures (by 1.6ppt to 21.9%).



In terms of the economic content of transactions, the highest growth in January-March 2011 against last year's indicators was noted in expenditures of the **State budget of Ukraine** for capital transfers (6.8 times), for payment of interest/income on obligations (2.3 times), for capital construction/acquisition (by 37.4%), and for current transfers to public administration bodies of other levels (by 27.8%). Expenditures decreased throughout Q1 2011 for "Subsidies and current transfers to enterprises (institutions, organizations)" by 59.1%, "Foodstuffs" by 27.4%, and for "Medicines and bandaging materials" by 14.4%. The share of protected expenditure items according to economic classifications amounts to 79.4% (see Chart 15), which is 5.0ppt more year-one-year.

The share of capital expenditures within the overall structure increased from 1.5% in January-March 2010 to 3.7% in Q1 2011. Also, their amount increased by Hr 1.6bn or 2.8 times year-on-year. In particular, the financing of capital construction/acquisition increased by 37.4% year-on-year, and that of capital repairs, reconstruction, and restoration grew by 57.3%. The amount of capital transfers from the State budget to local budgets increased by Hr 1.8bn or, as has already been mentioned above, 6.8 times against the Q1 2010 figure.



Protected items accounted for 86.8% of all **local budget expenditures by economic classification** (see Chart 16), which is 3.8ppt less year-on-year.

A 2.0ppt decline is noted in the share of expenditures for payroll with taxes in the structure of local budget expenditures, which is consistently the largest item from among all the local budget expenditures and which amounted to 45.6% in Q1 2011. The share of expenditures for current transfers to public administration bodies of other levels decreased by 3.5ppt to 1.6%, and expenditures for current transfers to the population rose 2.2ppt to 23.0%.

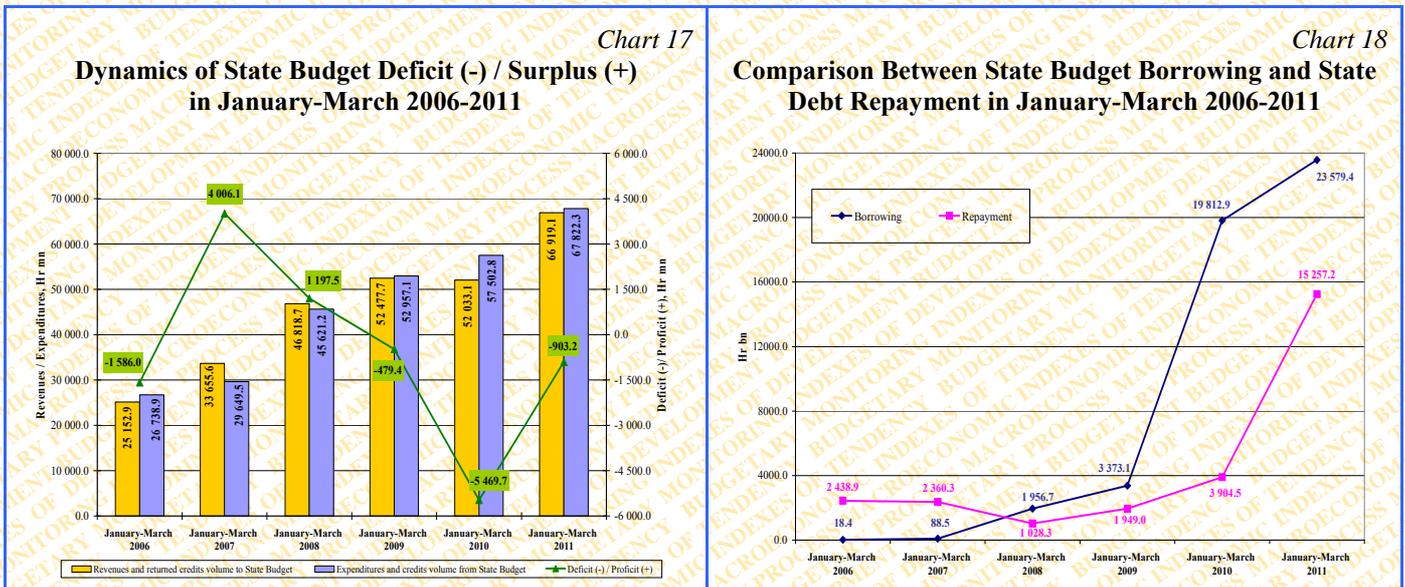
At the same time, the share of capital expenditures increased by 2.6ppt and amounts to 4.1% of all local budget expenditures. In nominal terms, capital expenditures were 2.4 times higher and amounted to Hr 1.6bn.

FINANCING OF THE STATE BUDGET

The main characteristic of the **State budget deficit** is its significant reduction compared to last year's figure (by 6 times or down to Hr 0.9bn) (see Chart 17). The deficit totaled 2.3% of the annual plan. The General Fund deficit totaled Hr 2.1bn (65.8% less than last year), and surplus of the Special Fund doubled to Hr 1.2bn. Borrowing exceeded repayment of the State debt by Hr 8.3bn in Q1 2011, which is 47.7% less year-on-year.

The borrowing growth rate was the lowest in the last three years year-on-year (19.0% compared to a 5.9 times increase in 2010, and 72.4% in 2009 against 2008). Internal borrowing totaled Hr 10.4bn and was mainly incurred through the issue of internal government bonds, of which Hr 5.0bn is intended for the capitalization of NAK Naftohaz Ukrayiny. External borrowing totaled Hr 13.1bn. A significant part of external borrowing consists of the 2011 issue of an external government bond (EGB) totaling \$1.5bn, as well as an additional 2010 EGB issue of \$100.0mn.

Debt repayment totaled Hr 15.3bn in Q1 2011, which amounts to 24.5% of the annual plan approved by the Law of Ukraine "On the State Budget of Ukraine for the Year 2011" (see Chart 18). The budget burden of repaying the debt obligations increased 3.9 times year-on-year. The repayment of internal debt totaled Hr 9.0bn or 24.1% of the annual plan, with the external debt repayment of Hr 6.2bn or 25.1% of the annual plan.



The situation regarding the use of borrowed resources improved for the better. Thus, the Hr 6.0bn borrowed for covering the deficit was used for current expenditures last year. This year, however, with the General Fund deficit of Hr 2.1bn, capital expenditures totaled Hr 1.0bn.

Receipts from the privatization of State-owned property totaled Hr 1.1bn or 10.9% of the plan approved for 2011. This is part of the earnings from sale of OJSC Ukrtelecom, which was privatized for Hr 10.0bn in March. These revenues were executed for Hr 0.1bn only in January-March 2010, or at 1.3% of the annual plan, and they were used as a source of accumulation for the Stabilization Fund.

The balance of budget funds totaled Hr 48.1bn at the end of March 2011, showing a total growth of Hr 8.7bn in the first quarter of the year. This balance increased 1.9 times year-on-year.

INTERGOVERNMENTAL TRANSFERS

Local budgets received Hr 20.1bn in intergovernmental transfers from the State budget (23.6% of the annual plan), which is 33.1% more than in Q1 2010. This raised the share of intergovernmental transfers in the total structure of local budget revenues to 52.0% against 47.1% in the respective period of 2010 (see Chart 19).

The amount of intergovernmental transfers remitted to the State budget of Ukraine by local budgets totaled Hr 615.6mn. (see Chart 20). Compared to the respective indicators of 2010, their volume decreased by 61.2% (nearly by Hr 1.0bn) and amounted to 1.6% of all local budget expenditures. These changes are primarily linked to a reduction in the planned amount of intergovernmental transfers to be remitted by the Kyiv city budget.

Chart 19
Dynamics of Transfers from the State Budget to Local Budgets in January-March 2006-2011

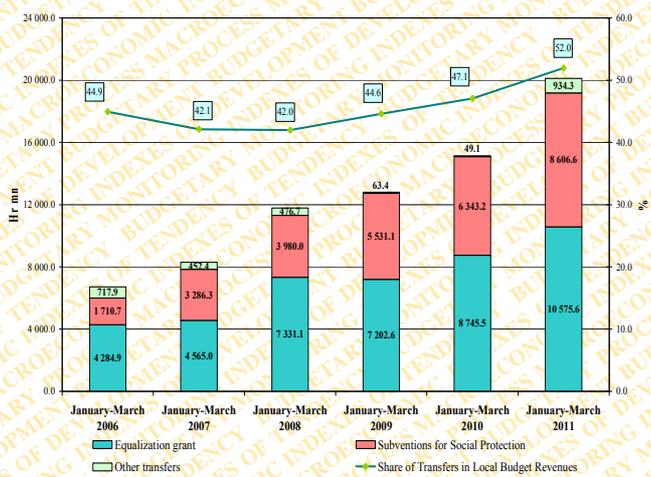
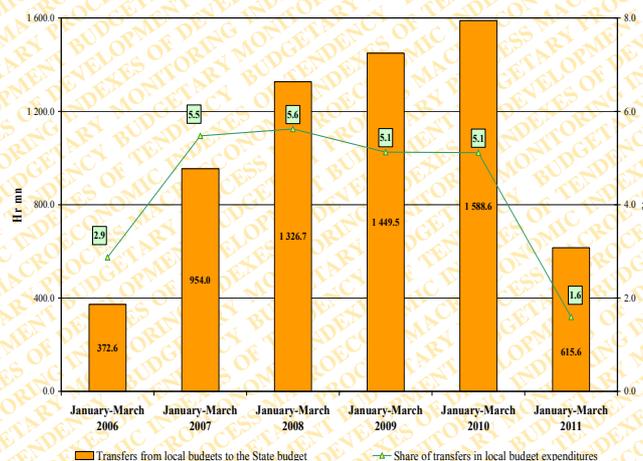


Chart 20
Dynamics of Transfers from Local Budgets to the State Budget in January-March 2006-2011



The equalization grant has the largest share in the structure of transfers from the State budget with 52.5%, which is 5.3ppt less year-on-year (see Chart 21 and Chart 22). An equalization grant totaling Hr 10.6bn was remitted to local budgets, which is 20.9% more than in Q1 2010.

Chart 21
Structure of Transfers from the State Budget to Local Budgets in January-March 2010

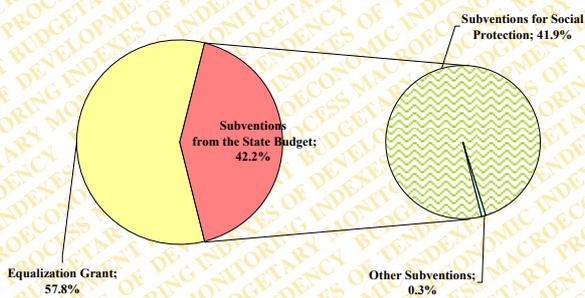
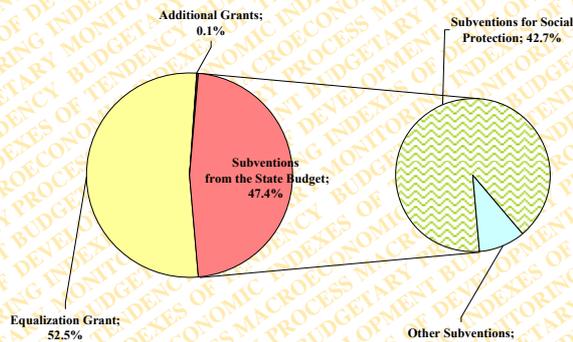


Chart 22
Structure of Transfers from the State Budget to Local Budgets in January-March 2011



The share of social protection subventions increased by 0.8ppt and amounted to 42.7%. In nominal terms, however, these subventions increased by 35.7% and totaled Hr 8.6bn. The share of other transfers remitted to local budgets from the State budget amounted to 4.7% against 0.3% in 2010, and their volume totaled Hr 0.9bn.

Based on the 1st quarter data, the levels of execution of annual targets for the provision of various types of intergovernmental transfers are as follows:

- the equalization grant was remitted at 24.3% of the plan;
- financing of additional grants varies from 0 to 18.2%;
- subventions for the social protection of the population were remitted at 24.3% of the plan;
- other subventions were funded at 14.9%.

This publication outlines the key trends in execution of the consolidated, State, and local budgets in January-March 2011. A more detailed information is contained in the publication *Budget Monitoring. Analysis of Budget Execution in January-March 2011* to be published in June 2011.